



IBA GLOBAL

August 2011

INSIGHT

Crisis point

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Euro on the brink:

A reprieve for Greece but dangers remain

Financial crisis:

Does the UK Vickers report have the answers?

Interview:

Peter Rees, Legal Director at energy giant Royal Dutch Shell

Business in

China: The risks of venturing outside Beijing and Shanghai



the global voice of
the legal profession*

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After graduating in 1952, Sandra Day O'Connor couldn't find a law firm willing to give her a job. Nearly 30 years later, she was the first woman appointed to the US Supreme Court, a historic milestone for women's rights. *IBA Global Insight* speaks to the former Supreme Court Justice who was at the centre of the controversial re-election of George W Bush.



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55 In America, firms compete for controversial and high-profile pro bono matters. In Asia, the same firms have been more pragmatic, tending to keep a low profile. But international law firms may have to strike a balance between commercial interests and the political passions of their Asian employees.

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From the Editor



Our cover line, 'Crisis Point', could sound like hyperbole. But, at a time when the Eurozone is wrestling with several economies on the brink of bankruptcy (see **Euro on the brink**, page 19), it seems to capture the mood at least. Meanwhile, America is attempting to come to terms with its own crisis, having run up \$14 trillion in debt (see **Uncle Sam and the New World Disorder** page 5). And Japan is confronting its own woes (see **The true meaning of too big to fail**, page 7). In these circumstances, perhaps 'Crisis Point' is an understatement.

At the same time, unique opportunities for change are currently being presented, by the Arab Spring, for example (see **Syrian regime will be forced to reform**, page 8). But, this comes at a time when the world's richest country is being forced to rein in its previously interventionist, but expensive, foreign policy as self-appointed 'global policeman'. Suffice to say, the global financial crisis that originated in the banking sector is having serious and widespread implications far beyond the purely economic and domestic.

Disappointing, then, that as carefully considered attempts to protect against another similar crisis emerge, such as the UK's Vickers report (see **Breaking the banks**, page 13), responses all too often focus on what the impact might be on parochial interests and competitive advantage. What the Eurozone has shown, most recently with its bailout of Greece, is the power of cooperative action. This though was crisis management. What's needed is a significant global shift. In a recent discussion, the IBA's Japanese President, Akira Kawamura, cogently conveyed the key role that the now fully globalised legal profession can, and should, be playing as they advise the world's major financial institutions. 'Safeguarding the people's well-being should be equally important to the international financial system,' he says, before adding that 'the traditional concept of the lawyer's competency might not work well.' The IBA's long-term work to develop new ethics guidance for the profession (see page 5) may start to focus minds in this respect.

James Lewis

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News



SKIP KALTENHEUSER

Is America's role on the world stage being written out? Or is the country simply being forced by new realities to call its shots more carefully, perhaps even enhancing influence and credibility assuming it makes the right calls? Ultimately, the projection of global influence comes down to wealth. When America goes broke, it really isn't all about the economy.

Many countries are stumbling under the weight of their challenges, after the finance sector ran roughshod over the globe. But none have taken on the world-class burdens the United States has. And some are proving very nimble in their priorities as a society, and will reap the rewards as America pays the price of domestic neglect.

Among those pushing for a more tempered foreign role is Michael Mandelbaum, director of the American Foreign Policy Program at the Paul H. Nitze School of Advanced International Studies (SAIS) at Johns Hopkins University. 'The growing fiscal burdens the United States will have to bear will impose restraints on foreign policy,' says Mandelbaum. 'In the coming cash-strapped era, I recommend that the country continue its active role in Europe, East Asia and the Middle East, while cutting back on the kinds of military interventions leading to nation-building that have become common in the post-Cold War era, from Somalia to Iraq.'

Mandelbaum notes that during the first two post-Cold War presidencies, the US militarily intervened in Somalia, Haiti, Bosnia, Kosovo, Afghanistan and Iraq. Motives varied, but the resulting nation-building efforts were frustrating – relevant institutions are not quickly created – and were not a hit with the US public.

The US role – often that of 'the world's de facto government' supplying services many governments can't – will be hamstrung by a loss of support from an increasingly strapped US public, says Mandelbaum. 'America will do less, and international relations will be transformed.'

This is an edited extract of a feature-length article assessing the impact of America's \$14trillion debt on its international role. The full-length article will be published in the next edition of *IBA Global Insight*.

Inaugural St Petersburg International Legal Forum brings together global leaders

IBA President Akira Kawamura recently participated in the inaugural St Petersburg International Legal Forum, where Russian President Dmitry Medvedev gave the keynote speech and former German Chancellor Gerhard Schröder moderated.

The event brought together leading experts in politics and law to discuss the legal issues involved in making economic systems more secure in terms of global development.

President Medvedev told delegates: 'Problems with enforcing laws, lack of respect for the courts and corruption are not just issues affecting our public life, but are macroeconomic factors holding back our national wealth growth and putting a brake on our efforts to carry out economic decisions and social initiatives.'

Mr Kawamura addressed the changing and increasingly important role of the legal profession in globalisation. He said: 'The legal service is no longer just the infrastructure of the economy or on the peripherals of business, but the main stream of the economic growth in the advanced countries.'

Read Akira Kawamura's full address at tinyurl.com/IBA-akira-stpetersburg.



IBA launches global ethics guidance for lawyers

Following years of work and discussion, the IBA Council has finalised a set of ethical principles for lawyers to follow across the world. The publication, *IBA International Principles on Conduct for the Legal Profession*, adopted on 28 May, presents ten principles to serve as a framework for the conduct of lawyers and promote the ideals of the legal profession. The principles covered include: independence; honesty, integrity and fairness; conflicts of interest; confidentiality and professional secrecy; clients' interest; lawyers' undertakings; clients' freedom; property of clients and third parties; competence; and fees.

James Klotz, Chair of the IBA BIC, said: 'We are hopeful that the IBA International Principles will serve as a basis for codes of conduct throughout the global legal profession and beyond. It is our aim that governments and other appropriate authorities in relation to furthering and improving the rule of law and defending liberty and justice will also realise the value of the core principles, so essential to the independence of the legal profession and democracy.'

He added: 'We believe that fledgling bar associations struggling to establish independence will find the principles a particularly great resource.'

The document evolved from the IBA's 'International Code of Ethics', passed at Council in 1988, which itself derived from an original Code passed in 1956. The initial idea was to update the 1998 Code, but the working party soon came to the conclusion a much wider revision was needed, as international law had progressed so far in that time.

Available on the IBA website, printed copies of the principles are also being distributed to all IBA members.



Portugal's bailout: a first step towards deep-rooted reform

SCOTT APPLETON

The bailout of Portugal by the 'troika' international institutions – the European Union (EU), European Central Bank (ECB) and International Monetary Fund (IMF) – may not be a cause for celebration, but it does at least bring certainty to the country's finances, say lawyers in Lisbon.

Following Greece and Ireland, Portugal became the third Eurozone country to seek a financial rescue package since the onset of the global financial crisis in 2007. The country's newly elected centre-right government, led by Prime Minister Pedro Passos Coelho, is now working on implementing a three-year agreement that will see funds worth €78bn committed.

Lawyers in Lisbon insist however that Portugal's troubles are neither the result of over-stated public finances nor a systemic banking failure, as was the case with Greece and Ireland respectively, but instead a lack of fiscal efficiency and competitiveness.

'Portugal is not facing structural difficulties but we must restructure our debts. A bailout is not desirable, but what it may finally provide is certainty to businesses, the capital markets and international investors,' says Diogo Leonidas, corporate partner with Garrigues in Lisbon, which is advising the IMF on the proposals.

More than looking for a quick fix to Portugal's economic problems, the planned structural economic and legal changes will have a deep-rooted impact. There is no doubt that the proposals, which include a restructuring of the financial system; the sale of the government's 'golden shares' in key companies; and a wave of privatisations and significant changes to tax, labour and redundancy rules, have the potential to make a significant difference to the state's finances.

Read the full article at tinyurl.com/IBAnews-portugal.

For further coverage of the crisis in the Eurozone see page 19

Best practices for cooperation among EU national competition authorities

A Working Group of the Antitrust Committee of the IBA has submitted a response to the draft best practices for cooperation among European Union (EU) national competition authorities, which the European Commission published for consultation on 28 May.

The best practices aim to foster and facilitate cooperation between those authorities in the case of mergers that are not subject to EU merger control and which require clearance in several Member States.

The Working Group welcomed the initiative, but flagged some concerns.

These include ensuring that the best practices should not result in an increased work burden on merging parties, and that they should not adversely affect timing, which is frequently key to merger transactions.

Working Group Coordination Officer Marc Reysen, partner at O'Melveny & Myers, said: 'The Antitrust Committee thought it important to let the European Commission have the benefit of the experiences of practitioners from different jurisdictions on how cooperation among authorities in merger control proceedings impacts the investigative process.'

'A particular focus of our submission therefore was on the practical aspects of such information exchanges, in particular on how they affect businesses and the way they relate

2011 IBA Bar Leaders' Conference: bringing corruption and money laundering to the forefront

Until the last decade or so, corruption was a recognised fact of doing business. Viewed as a means of cutting through red tape or surpassing competitors, corruption in business – or anywhere else, for that matter – was rarely discussed. Yet now there is a growing recognition of the negative impact corruption has on business, economies and development, and corruption is widely seen as a systemic global problem, not merely a private issue between parties.

As part of its on-going work in educating the legal profession on corruption-related issues, the IBA dedicated its 2011 Bar Leaders Conference to discussing the independence of the lawyer, the role of lawyers in preventing corruption, the cost of corruption and anti-money laundering issues.

Read more about the conference at tinyurl.com/IBA-BICconference and the IBA's anti-corruption project at: www.anti-corruptionstrategy.org.



to authorities. In a world in which parallel merger control investigations are becoming commonplace, the IBA – which can draw upon the experiences of members in various jurisdictions – is perhaps uniquely placed to address the issues that the consultation raised.'

Working Group member Guenter Bauer, partner at Wolf Theiss, added: 'We believe it is essential that the implementation of the European Commission's initiative does not lead to an additional burden on the undertakings concerned, neither in terms of the scope of work nor in terms of time required for the merger control review process in Europe.'

Download the full submission at tinyurl.com/IBA-antitrust-EUresponse.



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Tokyo Electric: the true meaning of too big to fail

PHIL TAYLOR

The Japanese cabinet has approved a rescue plan for Tokyo Electric Power Company (Tepco), the operator of Japan's Fukushima nuclear power stations. The plan seeks to avoid bankruptcy - and with it a politically devastating reduction or denial of compensation to accident victims.

'No government in Japan would ever want to be in a situation where it would say to victims that they will not be paid just because bankruptcy works that way,' says Mark Fucci, an Asia-based partner of Bingham McCutchen, which specialises in restructuring and insolvency.

Japanese insolvency law contains a variety of complex regulations and tends to favour business continuation rather than maximum value for creditors, with a court-appointed

trustee being given wide-ranging powers to deal with and liquidate the debtor's assets.

This difference from the Western approach to restructuring can cause problems. Unsecured creditors under the Japanese system do not enjoy the kind of rights available under the US Chapter 11 regime. A restructuring in the Tepco case would, therefore, inevitably involve haircuts for unsecured creditors in the continuing business.

Unless the law were changed, Fukushima victims would receive drastically reduced compensation, and Prime Minister Naoto Kan and his cabinet would face political suicide.

'Any haircuts to creditors under the proposed plan would have to be voluntary, and not formally imposed via a bankruptcy proceeding,' Fucci said. 'Perhaps the closest analogy is what the US government did with AIG.'

Read the full article at tinyurl.com/IBA-news-tokyo.

China: IP rights and wrongs

REBECCA LOWE

As China begins its seismic shift from industry to innovation, increasing attention is being focused on the importance of intellectual property (IP) rights. Yet some multinationals, it seems, remain to be convinced.

Chief concerns include the ingrained culture of counterfeiting and piracy in the country, and perceived local favouritism among judges operating in regional courts.

'If IP rights continue not to be respected or protected, you may find companies restraining themselves, or not expanding as quickly as they might otherwise,' says John Kamm, former president of the American Chamber of Commerce in Hong Kong and founder of human rights organisation the Dui Hua Foundation. 'No one is seriously considering shutting out China, but the pace and size of investments may be affected.'

China has long struggled to tackle piracy and the widespread counterfeiting of goods, which cost producers billions of dollars a year in lost sales. In 2009, the World Trade Organization upheld a US complaint that Beijing was violating trade

commitments by failing to combat piracy. This year, 70 per cent of respondents to the Business Climate Survey, by the American Chamber of Commerce in China, rated China's enforcement of IP rights as either 'ineffective' or 'totally ineffective'.

Yet few would deny that the IP landscape seems to be improving. Last October the Communist Party set up a dedicated IP enforcement office under the Commerce Ministry, and between 2009 and 2010 first instance civil IP cases filed in local courts rose by 25 per cent, according to a report by the Supreme People's Court.

Zhang Yi, a partner at Chinese firm King & Wood, admits that problems with the legal system remain, but stresses that these deal primarily with judicial inexperience and local law variation, which affect domestic as well as foreign companies.

'There is improvement in the enforcement. In most coastal areas we have set up a special bench - the IP Adjudicating Bench - where all judges only adjudicate IP cases. However, there are still outstanding IP issues to address, and the coastal area is much more advanced than inland cities.'

Read the full article at tinyurl.com/IBAnews-IPchina.

Nobel Peace Prize Laureate ElBaradei to speak at IBA Annual Conference

The Nobel Peace Prize Laureate, Dr Mohamed ElBaradei, will deliver the keynote speech at the opening ceremony of the 2011 IBA Annual Conference, in Dubai.



A seasoned diplomat, Dr ElBaradei served three terms as Director General of the International Atomic Energy Agency, an autonomous intergovernmental organisation under the auspices of the United Nations. In October 2005, Dr ElBaradei and the IAEA were jointly awarded the Nobel Peace Prize for their efforts 'to prevent nuclear energy from being used for military purposes and to ensure that nuclear energy for peaceful purposes is used in the safest possible way'.

In 2011, Dr ElBaradei emerged as a high-profile opposition figure in the Egyptian protests that culminated in President Hosni Mubarak's resignation.

For registration to attend, please visit: tinyurl.com/IBA-2011annualconference

Human rights news



Justice for Burma Campaign: the establishment of a UN Commission of Inquiry into international crimes

The IBAHRI Justice for Burma Campaign, launched on 12 July, calls urgently on lawyers to take action to galvanise support for a UN Commission of Inquiry (COI) into international crimes in Burma.

Burma is known as one of the most repressive regimes in the world. Murder, systematic rape, sexual violence, torture, the recruitment of children as soldiers, warrantless detention, widespread forced relocations and forced labour are all widely reported to have taken place. The UN Special Rapporteur on Burma has twice recommended the establishment of a COI into international crimes for Burma, but every call from the international community to investigate accusations of human rights abuses has been persistently ignored by the Burmese regime.

IBAHRI Co-chair Sternford Moyo said: 'Lawyers have both the legitimacy and duty to apply

influence and pressure where necessary to open an investigation when allegations of international crimes are reported. It is our inherent responsibility to uphold and promote the protection of human rights.'

The European Union (EU) will draft the forthcoming UN General Assembly (UNGA) resolution on Burma, to be introduced at the Third Committee of the UNGA by October 2011. The IBAHRI asks that EU Member States publicly support the COI and formally request the EU Commission to include it in the draft resolution.

The IBAHRI has produced a background paper and guidelines document providing information on simple actions that lawyers can take to make a great impact.

Further information and In-depth coverage of the on-going situation in Burma on the campaign can be found at tinyurl.com/IBABurmacampaign

Syrian regime will be forced to reform

REBECCA LOWE

Pressure is mounting on the Syrian Government to enact meaningful reforms after a series of violent crackdowns failed to dampen protests across the country, according to lawyers on the ground.

Demonstrations are growing every day, say witnesses, despite the death of a reported 1,400 people at the hands of Syrian troops and militiamen since the uprisings began in March.

'The protest is really gaining momentum, even though the security forces are quashing protesters more harshly,' says Samer Sultan, managing partner at Sultans Law, based in Aleppo. 'In rural areas, where the regime can't have security police in every village, there are protests every day.'

Violent clashes began on 18 March, as a team of delegates on a fact-finding mission for the International Bar Association's Human Rights Institute (IBAHRI) arrived to assess judicial

independence and the rule of law. A group of children were arrested for scrawling anti-government graffiti in the southern city of Daraa, triggering a backlash from residents. Security forces retaliated, allegedly killing three protesters.

At first, viewed as a potential force for reform, President Bashar al-Assad escaped the wrath of the masses. Now, four months of failed promises later, it is the president's face on the placards, his name synonymous with arrogance, corruption and repression.

'This is a protest about democracy and authoritarian rule,' says Dr Abdel Salam Sidamed, associate professor at the political science department at University of Windsor, Canada, and rapporteur for the IBAHRI mission. 'It is a war of wills, if you like.'

'But this repressive path is not something the regime can sustain. They have been using it for over three months, but they still haven't scared the people. Eventually they will have to accept that they have to do something.'

It is not the wording of Syrian laws that needs to change, lawyers stress, but

the practice. The Constitution is based on just principles, but is undermined by a corrupt judiciary and security service with no respect for the rule of law. Even the Syrian Bar Association, once a bastion of independence, has become beholden to the executive.

'The report produces clear recommendations to the Ministry of Justice, the Ministry of Social Affairs and the Syrian Bar Associations that are relevant, whatever happens in the future,' says Shirley Pouget, IBAHRI programme lawyer, who organised the mission.

'We urge the Syrian Government to take action by immediately putting an end to the repression against protesters and engage in a genuine process of political reform. Pledges are not enough.'



Coverage of this issue, including the IBAHRI's report, *Human Rights Lawyers and Defenders in Syria: A Watershed for the Rule of Law*, is available on the IBA website: ibanet.org



Venezuela moving towards 'autocratic regime'

REBECCA LOWE

The 18-month incarceration of a Venezuelan judge for lawfully releasing a man from pre-trial detention is a dangerous sign the country is 'moving towards an autocratic regime', a leading international lawyer has said.

Judge Maria Afiuni, arrested in December 2009 for freeing a banker facing corruption charges, should be released immediately in line with domestic and international law, according to Professor Carlos Ayala, former president of the Inter-American Commission of Human Rights.

Ayala's comments follow calls for Afiuni's release 'for the sake of justice and human rights' by left-wing scholar Noam Chomsky, a long-standing friend of President Hugo Chavez, who recently criticised the socialist leader for his 'assault' on democracy and the rule of law.

Speaking to IBA Global Insight, Ayala said: 'I think the situation in Venezuela is very worrisome, very complicated. This case shows the great deterioration of the protection of liberties, human rights and democracy. We are entering a situation where we seem to be moving towards an autocratic regime.'

In April 2011, the International Bar Association's Human Rights Institute (IBAHRI) released a report on the independence of the judiciary in Venezuela, entitled *Distrust in Justice: the Afiuni case and the independence of the judiciary in Venezuela*. The IBAHRI was the only international organisation to secure a meeting with Afiuni while under house arrest in Caracas.

Read the full article at tinyurl.com/IBAnews-afiuni.

ICC report on external communications

The latest IBA ICC Programme report, entitled *ICC External Communications: Delivering Information and Fairness*, examines public statements by ICC officials and related jurisprudential developments.

The report, published on 21 June, contains 20 key findings and recommendations. These include:

- Increased coordination between Court organs to integrate communications initiatives
- Harmonisation of messages in line with the one-court principle
- Adoption of court-wide guidelines and a policy on public statements during ongoing proceedings
- A revision of the content and frequency of ICC press releases

Mark Ellis, IBA Executive Director, said: 'Communication shapes the way the world views the Court and the legitimacy of its proceedings. When the Court speaks, messages must be clear and fair to all participants.'

The report, which was the fifth in a series of outreach reports from the IBA's ICC Programme, extensively evaluates the Court's public information and external communications policy from January 2010 to April 2011. The full document can be found at tinyurl.com/IBAHRI-ICCreport.

The 27-minute educational film covers some of the most pressing issues facing the ICC, including the presumption of innocence, fair trial guarantees and the right to counsel. Among the ICC experts interviewed were ICC President Sang-Hyun Song and Richard Goldstone, former chief prosecutor at the International Criminal Tribunal for the former Yugoslavia and the International Criminal Tribunal for Rwanda.



To view the IBA film on the International Criminal Court (ICC), In the Dock: Defence Rights at the ICC, go to tinyurl.com/IBAHRI-ICCinthedock.

IBA Media Law and Freedom of Expression Website



MEDIA LAW AND FREEDOM OF EXPRESSION

IBA MEDIA LAW COMMITTEE AND IBA HUMAN RIGHTS INSTITUTE



IBA has launched an expanded IBA Media Law and Freedom of Expression (MLFOE) website, which aims to create a strong global network to help media lawyers support and learn from each other.

The new website, a joint IBAHRI and the IBA Media Law Committee project, is a valuable resource and research tool for students, academics and all other interested parties.

Alongside 'Expert Opinion' pages hosting articles and commentaries on legal issues, the site provides information about current events and developments in the industry, discussion forums, an up-to-date news blog, and details on upcoming MLFOE events across the globe.



The MLFOE site is a member's site, but registration is free. Only members can submit a new resource to the site or use the discussion forums. To join and contribute visit mlfoe.org.



Thomas Federspiel

25 October 1935 – 25 May 2011

A large community of lawyers around the world remembers Thomas Federspiel with respect and affection and is sad at the news of his passing away at the end of May this year.

Having trained at the University of Copenhagen, Thomas was admitted to the Danish bar in 1964. Just five years later, at the very young age of 33, Thomas was admitted to the Danish Supreme Court, having, by then, been an associate at London and New York law firms. He gave major support to Danish and foreign businesses, never forgetting the traditional part of the legal profession - litigation - and he was a regular litigant through the years. For many years he was also honorary legal advisor to the British Embassy. It was an obvious advantage for him that he was fluent in four languages.

In 1969, he also became a name partner in the firm Per Federspiel - today known as Gorrisen Federspiel Kierkegaard - and it was at this time that he joined the International Bar Association.

During his time with the Association, he made a considerable contribution as an Officer. Madeleine May, former Executive Director of the IBA recalls: 'When Thomas Federspiel was elected President of the IBA in 1980 he was the youngest ever President and this record continues today. Thomas faced, almost immediately, three challenges - the wish of the sections to have more say in the management of the IBA, the holding of the IBA's first meeting in Eastern Europe, being that of the Section on Business Law's conference in 1981 in Budapest, and the first biennial or indeed any conference of the IBA in Asia (New Delhi) in 1982. Thomas's task was made harder by the fact that the IBA's staff at that time had just nine members, IBA Officers received minimal travel and office expenses and the only means of communication with the IBA office was by telephone or telex.

'The major event and major success of Thomas's time as President was the New Delhi Conference. Pre-conference problems included the refusal to issue visas to South African delegates, initially resolved by agreement that visas could be obtained via Mauritius but later restricted to those opposed to "apartheid". Following Israeli bombing of refugee camps in Lebanon, the Indian Prime Minister, Indira Gandhi, withdrew her consent to open the conference and the Government

directed that no Israeli delegates could attend. Thomas handled both problems with great diplomacy and led an IBA delegation, which eventually persuaded Mrs Gandhi to inaugurate the conference, which she did with great dignity.



Thomas also gained the agreement of the Bars of South Africa and Israel for the conference to go ahead. It was an enormous success, still talked about today, and led to many other IBA events in India.'

Kumar Shankardass, IBA President 1987-1988 also remembers the influence of Thomas Federspiel at the time. 'I first met Thomas Federspiel at the Council meeting in Sydney in 1978 and recall with deep gratitude the strong support he gave me and the invitation from the Bar Association of India to hold an IBA biennial

conference in this part of the world for the first time in 1982. Many members of the Council were apprehensive at the time that appropriate facilities for a large and prestigious conference might not be available in India. At the suggestion of Thomas, the then IBA President Neal McKelvey and Secretary General Jack Bracken, visited us in New Delhi and subsequently provided reassurance to the Council about the adequacy of New Delhi's facilities. Thomas, by then IBA President, presided with great distinction over the 1982 Conference and acquired numerous friends in India and in Asia generally, not only for the IBA but also for himself. There are many of us in the IBA who strongly believe that the New Delhi Conference firmly altered the image of the IBA from a North-American-European organization to a truly international representative organization for lawyers worldwide. Much of the credit for this important development in the history of the IBA must go to Thomas Federspiel.

Shankardass also says that 'the period of Thomas Federspiel's presidency was also notable for the initiatives taken for the formation of the IBA Educational Trust and the new Section on Energy Law. I must also say that I was always grateful to Thomas for his advice and guidance in subsequent years when I myself served as Vice President and later as IBA President.'

Thomas Federspiel continued to be active in the IBA for many years after his Presidency and attended almost every conference until his recent illness.



Whistling in the dark

The American government's attempt to strengthen financial regulation with whistleblower provisions is meeting with opposition from predictable quarters. Meanwhile, federal employees are being left all too exposed.

SKIP KALTENHEUSER

Government giveth and government taketh away. That's a decent synopsis of Washington's approach to whistleblower protections.

On the encouraging side, at the end of May, SEC commissioners issued final rules for its whistleblower programme in a 3–2 vote. The rules, complying with the Dodd-Frank Act, provide employees reporting wrongdoing with sizable bounties on penalties collected, similar to rewards under the False Claims Act, with protection against retaliation. Republican members dissented, perhaps not sufficiently chastened by the agency's missed cues about Bernie Madoff's Ponzi scheme.

The shriek from the Chamber of Commerce hasn't abated and business groups continue to try and whittle back such provisions. In a mid-July Senate hearing, Harvey Pitt, a former SEC chair under George W. Bush, said the programme, which does not require whistleblowers to report internally to a company before going to the SEC, 'threatens to undermine corporate governance, internal compliance and the confidence of public investors in our heavily regulated capital markets'. Pitt, not renowned for sharpening SEC enforcement during his tenure, didn't like much about Dodd-Frank, saying it would make financial regulation more bloated and less nimble.

But the experience of most whistleblower attorneys is that whistle-blowers generally

report concerns internally first, only venturing outside after being on the receiving end of retaliation. Indeed, the SEC can sweeten the reward pot if there is first cooperation with company compliance avenues. For the moment, SEC chair Mary Schapiro is leveraging people with first-hand knowledge to help make up for limited agency resources.

Meanwhile, protection of federal employees runs down a more byzantine path, splintered in arcane legal complexity depending on the type of employee.

For example, the need to strengthen protections for national security whistleblowers was underscored by a provision slipped into this year's Intelligence Authorization Act by the Senate Select Committee on Intelligence. According to Tom Devine, who heads the non-profit Government Accountability Project, the law would have permitted agency chiefs to punish current and even retired employees, if the chief decides an unauthorised disclosure was made, starting with scrapping their pensions. In essence, it would have stripped national security whistleblowers of all free speech rights. Senator Ron Wyden, (D – Oregon), put a non-secret, public hold on the bill until the provision was dumped. The Senate approved this at the end of May.

This summer, several dozen government whistleblowers wrote to President Obama seeking his help in reinvigorating protections

for federal employees that have been steadily undermined since the Whistleblower Protection Act of 1989. They point out that less than two per cent of whistleblower cases prevail before the US Merit Systems Protection Board, with equally poor odds for whistleblowers standing before the notoriously hostile US Court of Appeals for the Federal Circuit. The same court access provided to private sector employees is important for federal whistleblowers, including reviews by regional circuit courts and jury trials. Devine says that for federal whistleblowers, the goal is just to get back to even, after retaliation. Given bureaucracy's long memory, 'even' can prove extremely elusive.

President Obama has long voiced support of whistleblower protection, acknowledging the billions whistleblowers can potentially save. So has almost every person in Congress, including the new Tea Party crowd. Many see protections as alternatives to WikiLeaks disclosures.

There are near unanimous votes for the Whistleblower Protection Enhancement Act, (WPEA). Though some lawyers believe stronger protections in the diverse national security arena would still have to be pursued, the bill, now in its fourth incarnation, would make progress on a number of concerns. But a funny thing happens every time the law nears the goalpost. A secret hold is placed by a senator.

Devine says the holds were placed by Jon Kyl, (R-Arizona), and by Jeff Sessions, (R-Alabama). They are close to the Department of Justice, which under Bush opposed WPEA. In 2004, 2006 and 2008 the senators killed the bill on behalf of the DOJ, which is also tasked with defending agencies against whistleblowers.

In 2010, insiders say the hold was put on as a professional courtesy to the incoming new House leadership under Speaker John Boehner, (R-Ohio). There are longstanding cosy ties between old guard Republican leadership and federal agency barons, who protect their bureaucratic fiefdoms and are not keen on hidden agendas being exposed to public scrutiny.

According to a 2010 study on global fraud by the Association of Certified Fraud Examiners (ACFE), by far the largest block of initial detections of fraud is that originating from tips – in government it's 46.3 per cent. Four times more than by management review. In government, revelations from tips are three times those from internal audits and over nine times those from external audits. Surveillance and monitoring, police notification and confessions aren't even in the running.

Don't put your faith in technology: IT controls turn up half a per cent of big frauds. Tips also dwarf other discovery categories in not-for-profit and in private and public companies.

The ACFE notes that while tips are consistently 'the most common way to detect fraud, the impact of tips is, if anything, understated by the fact that so many organizations fail to implement fraud reporting systems.'

But tips can't be taken for granted. Studying employees' reporting behaviour over the last decade,

the Ethics Resource Center found that 41 per cent of those witnessing fraud or misconduct do not report it to anyone. The center sees convincing employees to step forward as a critical challenge.

Steve Kohn of the National Whistleblowers Center notes that the first whistleblower protection law was enacted in 1778. He quotes Supreme Court Justice William O Douglas, who wrote two centuries later that 'the dominant purpose of the First Amendment was to prohibit the widespread practice of government suppression of embarrassing information.'

This is a time of shrinking resources for federal agencies, including politically inflicted cutbacks. Whether in the private or public sector, or the interplay between them, there is no more cost-effective oversight than the encouragement of hip tipsters.

Skip Kaltenheuser is a freelance journalist and writer. He can be contacted at skip.kaltenheuser@verizon.net.

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Breaking the banks

As the world looks to international decision-makers to protect against another financial crisis, *IBA Global Insight* assesses whether the UK's Vickers report has the answers.

NEIL BAKER

Banking is as old as civilisation itself. In 14 BC the Chinese were using paper money written on stag skin; well before them, Babylonian monks were making recorded loans. But modern banking as we know it today was, arguably, first established in 17th-century London, when Italian merchants moved to the city to finance a boom in trade. To this day, London remains a global banking centre, which is why it – and Britain more widely – has been particularly hard hit by the financial crisis.

The country's national economic output last year was 4.5 per cent below its pre-crisis level and 10 per cent beneath where it would have been if its 2007 growth trend had continued. Unemployment has risen by more than 800,000 since 2007. And among its leading banks, more than 80 per cent of RBS and 40 per cent of Lloyds are in state ownership.

No wonder then that Britain has been so actively trying to learn the lessons from the crisis and to reduce the likelihood of something similar happening again. The last two years have seen an unprecedented level of activity by regulators and policy-makers, culminating with the Independent Commission on

Banking – known as the Vickers report, after its chairman, Sir John Vickers, a former Chief Economist at the Bank of England.

The Commission's interim report – published in April – underlines how hard it will be to provide any simple solutions to the problems that caused the crisis. Getting more control over banks is difficult, and doing so without undermining the global competitiveness of the UK financial sector is harder still. And, in any case, effective supervision of banking is, increasingly, a global problem that requires global solutions.

Banking review

When the government created the Commission last year it gave Vickers a clear brief: to find ways to reduce systemic risk in the banking sector; to mitigate moral hazard – where some banks are too big to fail; to reduce the likelihood and impact of a bank going bust; and to promote competition, especially where large banks are gaining competitive advantage from the expectation that government will bail them out if they run into problems. One issue

underpinned all of those questions: should banks be forced to separate their retail and investment businesses?

The Vickers report begins with a cogent analysis of what went wrong in the global financial sector. Both lenders and borrowers took excessive and ill-understood risks, and banks operated with excessive leverage and inadequate liquidity, it says. Regulators allowed banks to crank up the ratio of their assets to their capital base far too high – to twice normal levels – and when they needed market funding they could not find it. When the crisis hit, many bank balance sheets could not absorb their losses, and as institutions began to fail, the complexity of their market operations made it impossible to sort the good parts from the bad in an orderly way. To avert panic and ensure basic banking services continued, government had to step in.

One means of avoiding the need for such intervention in future is to force banks to separate their retail and investment operations. The Vickers report – in a very British compromise – argues that some form of separation is needed, but adds that ‘a balance must be struck between the benefits to society of making banks safer and the costs that this necessarily entails’.

Full separation – where banks are carved up and cross-ownership of retail and investment banks is restricted or banned – might give retail customers the greatest protection, and therefore minimise the need for government intervention, Vickers argues, but it would also remove many of the benefits of universal banking, whereby banks use their investment activities to provide cheaper services to retail customers. But on the other end of the scale, simply separating the operating systems inside a bank, so that a failing one can be broken up or fixed more quickly, would probably not be a big enough reform, the report says.

As a mid-way, the report suggests what it calls ‘retail ring-fencing’, whereby retail banking operations would be carried out by a separate subsidiary within a wider group. The idea at this stage – and full conclusions will be out in September – is that universal banks should maintain minimum capital ratios and loss-absorbing debt to cover their UK retail banking operations, as well as for their businesses as a whole. But as long as they don’t dip below those minimum levels, they will still be able to transfer capital between their UK retail and other banking activities. The proposal is that ‘systemically important’ banks and all retail banks in the UK should have a baseline ratio of equity:risk weighted assets of at least 10 per cent.

‘It is open to debate whether a retail ring-fence would give more or less banking stability

than full separation between retail banking and wholesale and investment banking,’ the report says. ‘It would be less costly to banks because they would retain significant freedom to transfer capital. The required UK retail capital level would constrain banks only when they wanted to go below it to shift capital elsewhere, say to their wholesale and investment banking operations. But at times of overall stress it would not be desirable for the leverage of UK retail banking operations to increase in this way.’

A threat to competition?

One of the report’s aims is to increase competition in the UK banking sector. A reduction in the implicit government guarantee enjoyed by systemically important banks will help, but will not be enough on its own, the report says. The big incumbent banks have few challengers and one of them – Lloyds – now holds around 30 per cent of current accounts. Vickers suggests a mix of measures to fix this. They include forcing Lloyds to sell a package of assets and liabilities (The European Commission has already called for this, but Vickers says Lloyds needs to do more) and reforms to make it easier for retail customers to move their accounts.

‘A balance must be struck between the benefits to society of making banks safer and the costs that this necessarily entails’

The Vickers report

Along with the proposed new capital rules, these reforms are what Vickers calls ‘a combination of more moderate measures’. They may not be as radical as a forced split between retail and investment banking, but they will entail costs to banks nonetheless. However, these costs ‘appear to... be outweighed by the benefits of materially reducing the probability and impact of financial crises,’ the report says.

One reason for the ‘moderate’ approach is that Vickers needs to shore up the UK banking system in a way that doesn’t harm its international competitiveness. Hence the report does not suggest that UK banks should have to meet higher capital standards than those agreed internationally, ‘provided that they can fail without risk to the taxpayer’. Indeed, it argues that its reforms ‘would support the competitiveness of the economy and would be likely to have a broadly neutral effect on financial services’.

That’s because they would affect only a

small proportion of the international financial services industry based in the UK, says Vickers, and, in any case, 'improved financial stability should be good, not bad, for the competitiveness both of the financial and non-financial sectors'. Countries that suffer from financial crises are less attractive places for international businesses to locate, it says,

'Banks are either separate or they are integrated in some way. Like pregnancy and death, you either are or you aren't'

Rob Moulton
Ashurst

so 'More resilient banks are therefore central to maintaining London's position as a leading global financial centre, not a threat to it.' A domestic taxpayer guarantee might help some banks to compete internationally, but 'it would be a fiscally risky subsidy without justification,' the report concludes.

Mixed reaction

The Vickers report – or at least its interim findings – garnered a mixed reaction, with many in the media opining that banks had been let off lightly. Bank share prices certainly strengthened on news that Vickers was not calling for a forced break-up of banks that were deemed too big to fail. But Vickers himself believes that the reforms outlined in his committee's report are 'far-reaching' and 'could be transformative'. At the press launch of his findings, Vickers dismissed suggestions that banks were getting an easy ride. 'I absolutely reject any notion that we bottled it,' he said.

But Ashurst regulatory partner Rob Moulton says the 'balanced route' taken by Vickers raises a lot of unanswered questions. 'The Commission has tried to chart a course between splitting up the banks and not disrupting their role. This is a difficult course to plot. Banks are either separate or they are integrated in some way. Like pregnancy and death, you either are or you aren't,' he says.

'How will the failure of the investment banking arm of a retail bank not impact upon the credibility of its retail operations, which depend upon continued public confidence? Will the proposal encourage banks to operate their main businesses from abroad, where no such restrictions apply, and conduct their UK operations from a branch in London?'

Nabarro corporate partner Alasdair Steele says Vickers acknowledges a lack of empirical data on whether the proposed reforms will drive major banks away from the UK, but then seems to dismiss the future risk of any such relocation. 'While the immediate impact of the loss of a major bank's headquarters may be relatively small, the long-term risk is considerably greater,' says Steele. 'New products and business lines are more likely to be developed from headquarters outside the UK, which over time will lessen the importance and influence of London as a financial centre.'

Norton Rose financial services partner Jonathan Herbst also questions the impact on competition. 'The decision not to go the whole way to require the splitting up of the banks is welcome but this half way house will only succeed if it is workable and does not leave the UK at a competitive disadvantage globally,' he says. 'The jury is still out on this'.

Law firm Olswang, in a client briefing note, said it doubted whether Vickers' proposals would have a neutral affect on the

Legal and regulatory responses to the crisis in the UK

The Banking Acts

The Banking (Special Provisions) Act 2008 was introduced as an emergency measure when the Northern Rock bank ran into difficulty. It gave regulators the power to take action with regard to troubled institutions before they had become formally insolvent and created a new insolvency procedure for banks. The Banking Act 2009 updated and extended the 2008 version.

Turner review

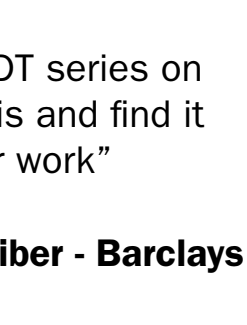
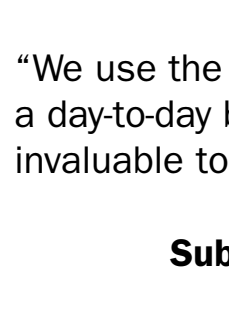
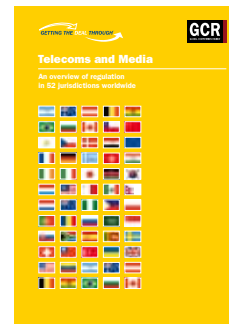
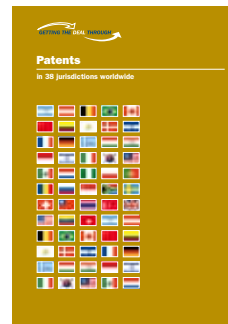
The Turner review, published in 2009, was a government-commissioned report from the head of the FSA on the causes of the financial crisis and how the UK regulatory system needed to change. It led to the FSA promising a 'fundamental shift' in its approach to regulation, so that it focused less on internal processes and more on business strategies and system-wide risks.

Walker Review

The Walker Review, also published in 2009, was a government-commissioned report on the quality of corporate governance in the UK financial sector. It made a series of recommendations on issues such as the role of the board chairman, the disclosure of executive remuneration and high-level processes for reviewing strategic risks. It also created a new stewardship code setting out the governance role of institutional investors.



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competitiveness of UK banks. 'Retail banks based in the European Economic Area [the European Union plus Iceland, Liechtenstein and Norway], which want to accept UK-based customers or establish branches here, do not

'On an international level there are serious doubts as to whether what has emerged so far represents a big step forward'

Hendrik Haag, Hengeler Mueller
Chair, IBA's Task Force on the Financial Crisis

need to operate through a UK subsidiary and a change in European law would be required to force them to do so,' it said. 'In consequence, the proposals are anti-competitive as regards the UK's position in the European retail banking market.'

International agenda

One thread running through the Vickers report is a recognition that the question of how better to regulate international banks is one that will require – largely – an international answer. This effort is being led by, among others, the Basel Committee on Banking Supervision, the European Commission and the G20's Financial Stability Board.

The European Commission has created three new supervisory bodies to oversee Europe's financial services industry and capital markets, including the European Banking Authority, which opened for business on January 1. Hector Sants, chair of the UK Financial Services Authority, said recently that Europe's national financial regulators will see their powers curtailed as these new supervisory bodies get up and running.

Commenting in the FSA's latest annual report, Sants said it was 'important to recognise the implications of the change', which will see the issues of most importance decided in Brussels. The new bodies will soon become 'the key policy-making forums' in Europe, said Sants.

But will this move to a new, more international regulatory framework have the desired effect? The IBA created a Task Force on the Financial Crisis to review global regulatory shifts and report on their impact. Some individual countries may have worked hard to fix their own national banking sectors, but 'on an international level there are serious doubts as to whether what has emerged so far represents a big step forward,' writes Task Force Chair Hendrik Haag, a partner at

Hengeler Mueller, in the task force's report. The regulatory organisations involved are 'too large and clumsy and not remote enough from the political process,' he says.

When the crisis broke, the expectation was that there would be a fast and radical change of bank regulation around the globe, according to Haag. 'One of the themes was that there must be a single regulator for global financial institutions to prevent a similar crisis from happening again. About three years later we are now looking at the first results of the reform process. There are very few elements that one could honestly call a radical change.'

One problem, says Haag, is finding ways to get national regulators thinking beyond their domestic interests. 'The *Lehman Brothers* case has shown that national regulators quickly become very self-centred in their thinking when it gets to repatriating or locking in funds necessary to preserve the liquidity of the parent bank or a subsidiary in their own country,' he says. 'This may be understandable, but it is certainly not always helpful. Better cooperation of national regulators based on clear cut rules negotiated beforehand would certainly be a great step forward.'

The world has become a better place in terms of less fragmented and better coordinated supervision of the financial industry, the IBA report says, but it is still far from being in a position to deal with the next crisis in a fundamentally more efficient manner, let alone to prevent one. 'The necessity of rescuing a too-big-to-fail institution with government help will not become a matter of the past soon,' writes Haag.

And that creates an interesting question: if there was – however briefly – enthusiasm among regulators and politicians for deeper reform, did the crisis create an opportunity that was quickly wasted? Haag says that isn't the case. 'While some of the proposals were squelched by lobbying from the banking industry and political debate between opposing parties, much of the compromise that has been found is based on the perception that an efficient and innovative financial industry is necessary for the wellbeing of the world economy as a whole. Too much regulation is likely to have a negative impact on the ability of the financial industry to perform that role.' And that is the difficult balance that Vickers' final recommendations will need to achieve. ☒

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Another bailout for Greece brings a reprieve, but the plight of Italy, Ireland and Portugal has the potential to push Europe and the global financial system further into turmoil. The consequences, should Spain catch the contagion, are unthinkable.

SCOTT APPLETON

The latest bailout for Greece in July may have earned temporary respite for the Eurozone. But, the bailout of Portugal earlier in the summer by the 'troika' of the European Union (EU), European Community Bank (ECB) and IMF (International Monetary Fund) may not be a cause for celebration though it has brought some certainty to the country's finances, say lawyers in Lisbon.

Following Greece and Ireland, Portugal became the third eurozone country to seek a financial rescue package since the onset of the global financial crisis in 2007. The country's newly elected centre-right government led by Prime Minister Pedro Passos Coelho is working on the implementation of a three-year programme that will see funds worth €78bn committed to the country.

A Memorandum of Understanding (Memorandum) drafted by the EU, ECB and IMF was agreed by all Portugal's major political parties ahead of the Parliamentary elections on 5 June, although the detail surrounding the implementation of the proposals has yet to be fully revealed.

'Many of the remedial measures included in the Memorandum were previously contemplated

but had always proved politically unattractive,' says Manuel Santos Vitor, Deputy Managing Partner of PLMJ, Portugal's largest law firm. 'We had reached a point where the domestic banks were unable to add further liquidity to the market and had stopped buying government debt, which itself had begun having trouble paying its own bills.'

Lawyers in Lisbon insist however that Portugal's troubles are neither the result of over-stated public finances nor a systemic banking failure, as was the case with Greece and Ireland respectively, but instead a lack of fiscal efficiency, competitiveness and fundamentally an inability to reduce public spending.

'Portugal is not facing structural difficulties but we must restructure our debts. A bailout is not desirable but what it may finally provide is certainty to business, the capital markets and international investors,' says Diogo Leónidas Rocha, corporate Partner with Garrigues in Lisbon, which is advising the IMF.

Memorandum

For too long, Portugal has been a minor player in a massive financial upheaval, believe many. Portugal's national debt currently stands at

around 83 per cent of GDP, although the budget deficit has fallen from 9.3 per cent of GDP in 2009 to 7.3 per cent in 2010, albeit with the domestic economy expected to shrink by up to two per cent this year.

A formal bailout request was made on 6 April shortly after the resignation of the former Socialist Prime Minister José Sócrates after a failure to win parliamentary support for a fourth austerity budget. At the time, yields on Government bonds had hit a record 7.7 per cent on ten-year issues and 8.2 per cent for five-year issues with Portugal needing to refinance an estimated €4.5bn of bonds later that month.

The troika has therefore made the 'difficult' decisions that Portuguese politicians had been previously afraid or unwilling to commit to. Funds will however only be released once the government meets the milestone targets set out in the Memorandum, which proposes far more than a quick fix to Portugal's economic problems. It sets out economic and legal reforms that will have a deep impact including a requirement for the government to privatise a number of major Portuguese companies, to sell its 'golden shares' in companies such as Portugal Telecom, recapitalise and restructure the banking system, renegotiate public works projects, change aspects of the tax, court and labour law systems, and reduce regional budgets.

The deficit must drop to 5.9 per cent in 2011, 4.5 per cent in 2012 and three per cent in 2013 to increase efficiency and national competitiveness. Targets have been set to reduce public spending on schools and healthcare and a proposed freeze on public sector pay and pensions until 2013, as well as a special tax on pensions over €1,500 a month. There are also proposals to reduce corporate tax and increase VAT and excise taxes.

'As a small and peripheral eurozone economy we cannot help but be tossed about in the storm,' says Francisco Sá Carneiro, partner with leading Lisbon banking and corporate firm Campos Ferreira Sá Carneiro & Associados.

Significant will be the way the government implements the planned privatisations, say lawyers. The airports operator ANA (Aeroportos de Portugal) and state airline TAP are scheduled for sale. In the energy sector, the government's preference and other holdings in companies such as Galp, EdP and REN are also to be sold, while there exists the potential to review existing renewable energy feed-in tariffs. Much of this is expected to happen by the end of the year.

The Portuguese Government had already announced the cancellation or delay of major

infrastructure spending – meaning no new Lisbon airport or third bridge over the River Tagus – but the Memorandum stipulates a moratorium on any new public-private partnerships (PPPs) and a reassessment and potential renegotiation of the 20 most significant ongoing PPP and concession agreements.

Financial preservation

A key aim of the Memorandum is to 'preserve financial sector stability, maintain liquidity and support a balanced and orderly deleveraging of the banking sector'. Portuguese banks had until the end of June 2011 to present medium-term funding plans, while the Bank of Portugal will impose a nine per cent tier one capital ratio by the end of the year, rising to ten per cent in 2012.

Up to €12bn will be made available to recapitalise banks as part of a €35bn issue of government backed bonds – although any institutions benefitting from equity injections will need to meet specific management commitments, following a general rise in regulatory scrutiny and stress testing. Nationalised Banco Português de Negócios must be sold without a minimum price, and state-owned Caixa Geral de Depósitos is to be streamlined – through the sale of its insurance arm and non-subsidiary operations, and a potential reduction of international operations.

'A bailout is not desirable but what it may finally provide is certainty to business, the capital markets and international investors'

Diogo Leónidas Rocha
Garrigues

But liquidity concerns extend well beyond Portugal's own banks. Spanish Government officials may remain confident that there is little risk of economic contagion but there are concerns over how the bailout will affect Spanish investors and businesses with interests in the country. As the biggest foreign investor in Portugal, Spanish banks and businesses have the most to gain or lose from the plans.

'Many investors can afford to remain clear of Portugal but for Spain the country remains strategically important, in order for businesses to expand their regional footprint and to open up further new market opportunities internationally,' says Jorge Santiago Neves,

a Lisbon-based partner with one of Spain's largest firms Gómez-Acebo & Pombo.

A number of foreign banks have already begun to limit their exposure to both the shrinking Portuguese economy and the tougher regulatory requirements of the bailout package, including potentially restructuring their operations as local branches rather than distinct Portuguese entities. Such a move would enable them to draw on the capital ratios of the parent bank and to avoid the need to raise extra local liquidity in Portugal. Foreign banks are now seeing increased deposits as Portuguese savers move away from the perceived more vulnerable domestic banks.

'Many investors can afford to remain clear of Portugal but for Spain the country remains strategically important, in order for businesses to expand their regional footprint'

Jorge Santiago Neves
Gómez-Acebo & Pombo

'After the elections we have begun to see businesses implement the moves required to either safeguard their interests or look to capitalise on the new opportunities presented in Portugal. We already see international investors monitoring events but no-one wants to commit until there is certainty as to what lies ahead,' says Santiago Neves at Gómez-Acebo & Pombo.

Firewall

Portugal's financial assistance package is intended in part to act as a 'firewall' to prevent contagion of the Spanish economy, the fourth largest in the eurozone. If it went into default it might call into question the stability of the entire eurozone, believe many. At the end of 2010, Spain's public debt to GDP ratio stood around 60 per cent, with a public deficit comparable to Portugal at 9.1 per cent, albeit but with the highest unemployment rate in the EU at 21 per cent.

Lawyers admit that there remains investor uncertainty over the future direction of the Spanish economy, but nearly all insist that it remains fundamentally sound. Events in Portugal may be distressing but more significant is the perceived strength of the euro as a whole and particularly the EU and ECB's ability to manage the uncertainties surrounding the Greek economy.

'Spain has suffered significant downturns before but around the time of the [first] Greek bailout, last May, there was a definite sense that Spain might go the same way. The result was a pause of activity particularly among international investors who took a 'wait and see' approach to how things would play out. Our domestic economy clearly faces challenges but we now see more positive signs internationally,' says Ignacio Ojanguren, Managing Partner of Clifford Chance in Spain.

Spain has nonetheless seen market yields rise on Government short and long-term bond offerings – peaking at 250 basis points above the benchmark German bund in recent weeks – but continues to raise funds on the international debt markets. Investor concerns may be subsiding but the summer months will prove a significant test of confidence in the country's capital markets and its financial sector.

A proposed first initial public offering of 2011, of 50 per cent of Atento (Telefónica's call centre operation) scheduled for mid-June has already been abandoned. More significant however will be the success of the proposed July IPOs of two of Spain's newest banks, Bankia and Banca Cívica, alongside the newly created CaixaBank, say lawyers.

All were formerly cajas (savings banks), although the past year has seen their number shrink from 43 to 17, encouraged by the Bank of Spain, following institutions' exposure to the collapse of the country's real estate market and the imposition of new capital adequacy rules. Alicante-based Caja Mediterráneo (CAM) has already been taken over by the state after the disclosure of a €2.8bn hole in its accounts – twice the €1.45bn shortfall calculated by the Bank of Spain.

Barcelona-based giant La Caixa has restructured as CaixaBank with a public listing completed on 1 July following a complex asset swap with its listed industrial holding entity Critería. The new bank has a market capitalisation of around €18bn, placing it among Europe's largest banks, and the listing came days after Bankia and Banca Cívica published the details of their sharply discounted listing plans.

Bankia is the product of the merger of seven cajas: Caja Madrid, Bancaja, La Caja de Canarias, Caja de Ávila, Caixa Laietana, Caja Segovia and Caja Rioja. Led by former IMF Chief Rodrigo Rato, it is now one of Spain's largest domestic banks and hopes to raise around €4bn from a mid-July float. It will be closely followed by Banca Cívica – the product of the merger of Cajasol, Caja Navarra, Caja Canarias and Caja de Burgos – which intends to raise around €850m. Also lined up for an

IPO later in the year is Banco Mare Nostrum, a merger of Caja Granada, Caja Murcia, Caixa Penedès and Sa Nostra.

A key benefit of the restructuring of the cajas has been to enable them to secure private investment and to operate internationally. The desire of many new banks is to emulate Spain's leading listed institutions Santander and BBVA, both of which have emerged relatively unscathed by the domestic financial crisis, largely because a significant share of their revenues is now generated outside of Spain (and Portugal).

Santander last year undertook the globe's largest IPO capitalising on Brazil's economic boom by raising €5.4bn for a 14 per cent stake in its local subsidiary Santander Brasil. It has this year already acquired one of Poland's leading banks Zachodni WBK and is reportedly preparing plans to float its enlarged UK operations, which combines banks that failed or were failing as a result of the financial crisis. BBVA is the owner of Mexico's largest bank BBVA Bancomer and has this year acquired a stake in leading Turkish bank Garanti for €4.2bn.

No guarantees

The situation in Spain may be less precarious than in previous months but there are however no guarantees over an economic upturn. There continues to be a slowdown in consumer spending, a stagnant real estate market (with a glut of properties built during the bubble of the past decade), rising bad loans for the country's banks, and record youth unemployment – prompting street demonstrations by thousands of people (*los indignados*) in cities including Madrid and Barcelona.

The national government may be regarded internationally as making the 'right' moves in trying to turn around the economy – cutting debt and reducing public spending – but the public finances of Spain's 17 Autonomous Communities continue to cause concern. Bilbao is reportedly the only city in Spain to be debt free, while a recent bond auction of local government debt managed by Santander reportedly raised only 50 per cent of the target amount.

'The biggest immediate test will be the success of the listings of the former cajas. If all goes well, Spain and its financial

institutions will begin to be back on track. If the IPOs fail, even at heavily discounted prices, then the recovery will take longer and the doubts that surrounded the strength of the economy at the time of the original Greek bailout, last May, could return,' says Ojanguren.

There is a perception in Portugal also that the new government has a relatively narrow window of 'opportunity' to bring the country back on to the path of financial stability and economic recovery. Prime Minister Passos Coelho is however already looking to go beyond the requirements of the Memorandum. In his debut Parliamentary address he announced plans to halve the annual traditional Christmas tax bonus, saving an estimated €800m,

equivalent to a third of the deficit reduction target for 2011.

'If Portugal were a company, we would have to refine our levels of service, ensure that revenues were properly accounted for, and develop new strategies for a changed world. We basically have to spend less and achieve more,' says Santos Vítor at PLMJ.

Ignacio Ojanguren
Clifford Chance

'Spain has suffered significant downturns before but around the time of the Greek bailout, last May, there was a definite sense that Spain might go the same way.'

But systemic issues remain to be addressed including in the area of justice. The inefficiency of Portugal's courts was identified by the Memorandum as a significant barrier to the timely enforcement of disputes – with greater alternative dispute resolution methods proposed – while law firms should also have greater freedom to promote themselves, it proposes.

'Nobody wished for the current situation but at least we do now have an economic recovery plan. The challenge for businesses is to assess what lies ahead, to adapt to the changes or to capitalise on any new opportunities presented,' says Santiago Neves at Gómez-Acebo & Pombo.

The election of Portugal's new government is therefore just a first step in an anticipated long and difficult process of change. But the hope is that success in Portugal should help to ensure economic stability across the Iberian peninsula. For the sake of the eurozone, Spain is 'too big to fail'. ☒

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Tech bubble 2.0

The successful flotation of LinkedIn and the purchase of Skype by Microsoft may suggest tech companies have come of age, or is another tech bubble on the way?

JONATHAN WATSON

Tonight we're going to party like it's 1999,' says one of the best-known songs by the artist formerly known as Prince. One person probably doing exactly that at the moment is internet entrepreneur Reid Hoffman, whose business networking website LinkedIn made an extraordinarily successful debut on the New York stock exchange in May 2011.

The company, founded by Hoffman in 2002, raised \$353 million through an IPO that valued LinkedIn at \$4.3 billion. This was more than double the \$175 million that the company said it expected the offering to raise. Soon after the flotation, its value soared to more than \$10 billion. This made LinkedIn the highest valuation of a US internet firm since Google raised \$1.7 billion in 2004. Pretty impressive for a company that made a profit of just \$15.4 million on revenues of \$243 million in 2010.

Earlier in May – the day after LinkedIn set the terms of its IPO – Microsoft said it was buying internet calling and video service Skype for \$8.5 billion. The price, three times more than its valuation at the end of 2009, raised eyebrows. Why pay ten times the company's revenue for a business that has changed hands

many times, never made money, and comes with substantial debt? Peter Bright, an analyst for technology news service Ars Technica, described it as 'a deal that's hard to understand'. One could argue that this is analyst-speak for 'crazy'.

The LinkedIn IPO in particular brought back uncomfortable memories of the bubble in technology stocks that took hold at the end of the last century. LinkedIn's

\$10 billion valuation was 40 times the sales it achieved in 2010, a multiple 'as silly as any in the late 1990s dotcom frenzy', wrote Nils Pratley, financial editor for UK newspaper the *Guardian*. 'It implies explosive growth for years and years and years... what are they smoking?'

According to Bart van Reeken, head of the information, communication and technology practice at De Brauw Blackstone Westbroek and Co-Chair of the IBA's Technology Law Committee, the LinkedIn IPO 'shows a marked belief in a yet-to-be-developed earnings model, which in my opinion is a clear sign of a bubble'. However, he does not feel quite the same way about Microsoft's acquisition of Skype. 'One must assume Microsoft is not buying Skype for resale but for integration into its business; the sale price reflects Microsoft's strengths at least as much as the value of Skype and is thus not in itself indicative of a bubble,' he told *IBA Global Insight (IGI)*.

One lawyer contacted by *IGI* argued that the acquisition of Skype was a clever piece of business. 'The \$8.5 billion was doing nothing sitting in Microsoft's bank account,' the lawyer said. 'There's no point giving it back to the shareholders, because that would make no difference to the share price, and they can build it into their mobile platform, which is where that feature has to be. I don't think that acquisition can be used as evidence that there is a tech bubble.'

Vagn Thorup, a partner with Kromann Reumert in Denmark and Co-Chair of the IBA Technology Law Committee, believes there is a short-term 'price bubble' but not necessarily the beginning of a tech bubble. 'LinkedIn achieved a high price because social media platforms are growing in importance, and

no one wants to be left behind,' he told *IGI*. 'Things can change very fast in the technology market. Look at Nokia – it dominated the mobile handset space until about five years ago but is now the shadow of its former self. The old players want to make sure they don't miss the boat.'

Thorup does not expect a repeat of the previous bubble, which was characterised by 'a large number of start-up companies appearing and suddenly exploding or imploding'. Technology companies launching IPOs in the coming decade will be 'big players operating well-established sites, not new names with unproven business models,' he says.

Yvan-Claude Pierre, a corporate and securities partner with DLA Piper in New York, also believes that LinkedIn's valuation was driven by investors' fear of missing out. 'When Amazon went public, there was a lot of scepticism at first, but that company has performed well,' he told *IGI*. 'Because of successes like that, people are willing to invest at a premium in certain sectors, including technology and the internet. The successes that have happened mean people don't want to miss out on any available opportunities. The big players are trading up and pricing high.'

Victor Shum, corporate and securities partner with Jeffer, Mangels Butler & Mitchell in San Francisco, does not think a new IPO boom is under way. 'There is simply a lot of excitement about internet and social media IPOs because

the IPO window has been closed for so long,' he told *IGI*. 'The difference between many of the companies now compared to the dotcom era is that most of the companies today have revenues and profits. Back in the dotcom era, people were more interested in eyeballs.'

As for the high valuations, Shum believes the public market will have limited patience for a company to grow into its valuation. 'At some point, its valuation must confirm to fundamental market metrics,' he says.

Recent signs that the market's enthusiasm for technology stocks is cooling seem to confirm this point. Although LinkedIn has performed well since flotation, others have achieved mixed results. Renren, a social media firm often described as 'China's Facebook', debuted on the New York Stock Exchange in May and raised \$743 million. However, the shares are now trading below their initial price of \$14. US mobile and web streaming music group Pandora Media saw its shares rise by as much as 60 per cent on its debut trading day in June, only for them to fall back below the IPO price the very next day. Pandora has yet to make a profit in the decade since it was



Am I hot or not?

Some of the privately owned companies technology investors would love to get their hands on

FACEBOOK

'Without a doubt, Facebook will be the most hotly anticipated stock debut at least since Google, and maybe ever,' said one recent article in the *Wall Street Journal*. People close to the company believe it is growing fast enough – it has now signed up more than 600 million users – to justify a valuation of \$100bn or more when the company goes public, possibly in the first quarter of 2012. Although founder Mark Zuckerberg has been non-committal, Facebook's chief operating officer Sheryl Sandberg has said an IPO is inevitable. However, there have been suggestions recently that the number of people using Facebook is falling in markets like the US, UK, Canada and Norway.

TWITTER

Twitter, which allows users to send short, 140-character text messages ('tweets') to groups of followers, is one of the internet's most popular social networking services and had 175 million users by the end of September 2010. However, co-founder Biz Stone said earlier this year that Twitter had no plans to go public any time soon and did not need additional funds, because it is making money. The company, created in 2006, employs about 350 people. In December 2010, Twitter said it raised \$200m in a deal that valued the company at \$3.7bn. Silicon Valley venture capital firm Kleiner Perkins Caufield & Byers was the lead investor, which included existing Twitter investors.

GROUPON

The loss-making discounts website says it intends to raise \$750m on the US markets at a price that could value the two-and-a-half-year-old company at more than \$20bn. However, Sucharita Mulpuru, an analyst at Forrester Research, said in an open letter that there is 'no rational math that could possibly get anyone to the valuation Groupon thinks it deserves'. He estimates its true value, based on financial information released with its flotation proposals, at closer to \$2bn. Last December Andrew Mason, the 30-year-old founder of Groupon, rejected a \$6bn offer for Groupon from Google.

founded, and about half of its sales revenue is used up by fees paid to music companies.

In general, tech IPOs have outperformed in first-day trading in the US this year, with an average jump of 24 per cent, according to research firm Dealogic. However, they are up just 15 per cent in trading since their IPOs. By contrast, US healthcare deals are on average up 23 per cent since their IPOs, despite a first-day jump of just 12 per cent.

How times have changed

John Kay, *Financial Times* columnist and a visiting professor at the London School of Economics, believes the key difference between the dotcom frenzy of the late 1990s and the present day is that the tech businesses being floated today are real businesses – even if they are quite small businesses – with customers and revenues. ‘However, they have the bubble characteristic that many of the people buying these stocks are buying them in the hope that they can sell them fairly quickly at a higher price to

somebody else, not because they are expecting to realise the cash flows that these businesses will ultimately generate,’ he says. ‘Viewed in these terms – the values of the cash flows they might generate – the valuations seem as absurd as the valuations in the tech bubble.’

Pierre notes that technology companies are stronger than they were a decade ago, not only from a financial perspective, but also from a brand perspective. ‘Technology companies with strong brands, wherever they are located, are very interesting to investors globally,’ he says. ‘It’s reassuring for investors to know that everyone recognises LinkedIn and that there is a high probability that new users will utilise the services it provides in the future.’

Another key difference between the late 1990s and now is that the technology industry is much more globalised. Many more internet-based businesses based in countries like China, Russia and

Israel are bound to come to market in the coming decade. Reports suggest that following LinkedIn’s debut, Russian internet company Yandex decided to raise its price guidance for its planned New York flotation. There are claims that Yandex, founded in 1997 and

often described as ‘the Google of Russia’, will sell shares on the NASDAQ exchange at between \$24 and \$25, higher than the previously planned range of \$20–\$22.

At the higher range, a Yandex IPO could raise \$1.3 billion, valuing the company at up to \$8 billion. Those prices would make the IPO the biggest by an internet company since Google and draw comparisons with Chinese search engine Baidu, whose shares leapt 354 per cent on its debut in August 2005. Yandex controls 65 per cent of the Russian market for internet searches, far outpacing global leader Google. Its earnings rose 90 per cent last year to \$135 million on sales that grew by 43 per cent to \$445 million.

Russian President Dmitry Medvedev has made his country’s ambitions clear by placing strong emphasis on his plan to turn the village of Skolkovo into Russia’s version of Silicon Valley. He hopes that eventually, more than 40,000 people will live and work in the area, which has been designated ‘Innograd’ (a contraction of the Russian for ‘Innovation City’). It

should act as a focus for a mass of Russian – and, if it takes off, multinational – high-technology companies. Medvedev initially approved the project in February 2010, although its development may depend on whether he wins another term in the 2012 presidential election.

‘The technology landscape appears to be more global, with Asia included, while it was much less so last time around,’ says van Reeken. ‘In addition, the offerings now include countries with a significant political risk. Moreover, there appears to be a larger risk that pension funds and other institutional investors are now buying into the bubble, too. All this may make the bubble even riskier than the last time around, and the potential consequences dearer – and more likely to fall on those not making the investment decisions.’

Mind your language

A new IPO boom in the technology sector would not have major implications for the work lawyers do, van Reeken says. ‘An IPO boom primarily means more IPO-related work and does not necessarily cause that work to change much,’ he told *IGI*. ‘Although this time, to protect themselves and their clients, lawyers are likely to be

‘Social media platforms are growing in importance, and no one wants to be left behind.’

Vagn Thorup

Kromann Reumert

Co-Chair, IBA Technology Law Committee



even more explicit in the warnings to be included in prospectuses. This shifts more of the risk to such buyers, which they appear to be happy to take.'

Shum believes that lawyers and law firms are much more conservative than they were ten years ago. 'There is still a lot of nervousness about the general state of the US and world economy which directly translates into the state of the legal profession,' he says. 'The number of attorney lay-offs and law firm implosions are still too fresh in many people's minds to make

international trade was going to be a big deal was right,' he says. 'The idea that the railways were going to make a big difference in the 19th century was right. Radio and television were big things in the 1920s. What happened in all of these was that people absurdly exaggerated the pace and extent of these developments – which also happened in the internet bubble.'

The other typical characteristic of a bubble is the exaggerated extent to which investors believe benefits will accrue to particular companies, rather than consumers. 'The truth

'The LinkedIn IPO shows a marked belief in a yet-to-be-developed earnings model.'

Bart van Reeken

De Brauw Blackstone Westbroek; Co-Chair, IBA Technology Law Committee

them believe that happy days are here again. Law firms today are more interested in getting paid cash for their services and any equity investment they may have made would just be considered a bonus.'

As always in the legal profession, attention to detail is crucial, says Pierre. 'At one point during the dotcom boom there were just so many deals that it was very difficult to keep on top of everything,' he says. 'There is also now a heightened level of due diligence and a flight to very experienced lawyers who know the sector well because people are very careful about global transactions and want more certainty that the deal is done correctly. Underwriters are prepared to spend to make sure they have dotted their 'i's and crossed their 't's.'

One thing worth remembering, says John Kay, is that bubbles do not start for no reason. One of the lessons of all stock market bubbles is that there is almost always something real behind them. 'In the South Sea bubble, the idea that

is in all of these things, whether we talk about trade or electricity or railroads, the reality of a competitive market is that most of the benefits go to consumers rather than shareholders,' Kay says. 'People often neglect that point. Too often in the dotcom boom, the purpose of the exercise was to take money off gullible investors, not to build real businesses'.

Despite that, the dotcom boom did produce a handful of real businesses. Now it seems a second wave of even stronger technology companies is ready to emerge from the wreckage it left behind. ☒

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Time to confront the past

Brazil is a vibrant democracy and its thriving economy is poised to overtake that of the UK. The country is looking ahead to 2014 and 2016, when it will host the football World Cup and the Olympics, respectively. So, why is the country launching a potentially agonising 'truth commission' on human rights abuses that were committed over 25 years ago?

BRIAN NICHOLSON

So, is this about the past, the present, or the future? At first sight, Brazil's somewhat tardy decision to formally investigate human rights abuses committed during the 1964–85 military dictatorship might seem to be of essentially historical interest. After all, the worst period of repression in the early 1970s is almost as distant for today's school children as the First World War was for baby boomers.

The Brazil of 2011 is a far cry from the dismal, brutal and frequently fearful place that your correspondent first visited in 1976. Back then, the army settled political debate by simply closing Congress. Students said 'yes, sir' to soldiers in the street, and police goons frequently clubbed or even shot labour leaders. Military censors sat in newsrooms.

Today Brazil is a vibrant democracy; imperfect, of course, but where isn't? The country's first woman president, a former leftist guerrilla, takes the salute from apparently obedient generals. There are so many parties and elections that people are getting fed up. So why start digging up skeletons, perhaps quite literally? And why now, of all moments, when the country is celebrating its acceptance into the ranks of major players, with the economy poised to overtake that of the UK in just a few years? Why now, when inequality is falling and many millions are enjoying their first credit cards and mobile phones? Why spoil the party

when the 2014 World Cup and 2016 Olympics are just around the corner, and construction of shiny new stadiums and airports seems to be top priority?

Might it be happening now, so long after the events, because President Dilma Rousseff – who took office in January – was herself captured and tortured in the early seventies, and so might have a greater personal stake in the matter than her predecessors? Lawyer Belisário dos Santos Jr, a former president of the Association of Latin-American Lawyers for the Protection of Human Rights, and currently Brazil's representative on the International Commission of Jurists, rejects such simplistic rational: 'We [human rights groups] have already done much to restore Brazilian history, but we had not attempted to use a truth commission. It's an instrument that has matured a lot recently, with experiences such as South Africa.'

Indeed, some 40 countries have used similar bodies, and the proposal for Brazil's commission was included – after long debate – in the Third National Human Rights Program sent to Congress last year by Rousseff's predecessor. It is now under examination in congressional committees.

If the bill passes as it stands, the commission will comprise seven Brazilians 'of recognised honesty and ethical conduct, identified with the defence of democracy and respect for

constitutional institutions, as well as the respect for human rights.' Chosen by the President, they will have a modest stipend, two years and a support staff of 14 to investigate grave violations of human rights and the structures and institutions that allowed these to happen, and to make reports and recommendations. The period is too short and the staff far too small, says dos Santos, and much will ride on the choice of nominees.

By the gruesome yardstick of some other Latin American countries, Brazil's ardently anti-communist Cold War military dictatorship was relatively tame. Human rights groups list 'just' some 400 dead or missing. Estimates in Argentina range anywhere from 9,000 to 30,000, in a nation four times smaller. And of course, thousands more in both countries were tortured, mistreated or otherwise deprived of their political, civil or human rights.

In Argentina, demands for truth about the 1976–83 'Dirty War' quickly led to investigations and subsequently, appalling revelations of babies stolen and torture victims tossed live into the sea from planes. Top generals were tried and jailed; various military units attempted armed insurrection; and the country implemented and revoked several amnesties. Trials still occur.

Brazil has tried no one. It enacted an amnesty in 1979 as its own military dictatorship was winding down. The law appeared to cover both sides: those who fought the dictatorship, and those involved in the torture or killing of prisoners. It has been endorsed by all subsequent governments and upheld by the Supreme Court. However, last November, the Inter-American Court of Human Rights condemned Brazil for failing to investigate the 'forced disappearance' of 62 people during army actions against guerrillas. In a summary of its ruling, the Inter-American Court of Human Rights said: 'the provisions of the [Brazilian] Amnesty Law that prevent the investigation and punishment of serious human rights violations are incompatible with the American Convention [on Human Rights] and lack legal effect...'. As such, the Amnesty Law 'cannot continue to represent an obstacle

for the investigation of the facts of the case or for the identification and punishment of those responsible.'

Earlier this year the Brazilian Bar Association (OAB) petitioned the Supreme Court to reconsider its position on amnesty in the light of the Inter-American Court of Human Rights ruling. The OAB also asked Rousseff to act. However, in June, the Attorney General's office said the government saw no reason to review Brazil's position, arguing that the country

signed and ratified the American Convention on Human Rights in 1992, and recognised the jurisdiction of the court in 1998. The 1979 Amnesty Law therefore precedes Inter-American Court of Human Rights jurisdiction.

However, dos Santos says that the IACHR, rather than calling for repeal of Brazil's Amnesty Law, was arguing that it cannot be applied to state-sanctioned torture and murder because these constitute crimes against humanity, and as such, cannot be amnestied: 'Brazil voluntarily accepted the competence of the Inter-

American Court of Human Rights, so it has no judicial grounds for not complying.'

According to dos Santos, Brazilian institutions are now strong enough to assimilate the formal investigation and prosecution of anybody responsible for torture and murder of prisoners; a step he sees as important to building a better democracy. He also believes that torture is not merely of historical interest – it is still widely used in Brazilian police stations. ☒

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'Human rights groups have already done much to restore Brazilian history, but we had not attempted to use a truth commission. It's an instrument that has matured a lot recently, with experiences such as South Africa.'

Belisário dos Santos Jr
Brazil's representative on the
International Commission of Jurists

The International Bar Association's Human Rights Institute (IBAHRI) is launching a programme to encourage Brazilian lawyers and authorities to be more proactive in working against the use of torture.

For more information on the programme, contact IBAHRI Senior Project Lawyer Alex Wilks at alex.wilks@int-bar.org or go to: tinyurl.com/IBAHRI-Brazil.



Peter Rees QC

Legal Director, Royal Dutch Shell

As well as sitting on the Executive Committee, Peter Rees oversees a team of 1,000 people in 50 locations, including the Ethics and Compliance function. This wide-ranging interview, conducted by James Lewis, covers issues, including the new world of anti-corruption legislation, business in Nigeria, and changes at Shell.

JAMES LEWIS: You've said that this is one of the best legal roles in Europe. What is it particularly that is special about this role from your point of view?

PETER REES: Well, I think it is a combination of things but it is a unique role, ultimately not only for the size of the legal department which you just mentioned, but also for the spread of the work that we do; the number of locations we are in as a legal team and of course the nature of the business that Shell is involved in. The oil and gas business going forward in the next couple of decades has a huge number of challenges but also a huge number of opportunities, and dealing with those is going to be something that our legal team will be able to get a huge amount of enjoyment from and add a huge amount of value to.

From my perspective as well and importantly, the Legal Director is part of the Executive Committee at Shell and therefore you are right in the middle of the business-making decisions which will be shaping the future of the Company. And that I think, combined with all of those other factors, makes the job unique and incredibly attractive, so far as I am concerned.

JL: You mentioned there, complexity, the scale – we're talking about 93,000 or so employees in however many countries, a hundred countries. How do you and your team deal with the complexity of issues and the sheer scale of the operation at Shell?

PR: We try and get as close as we can to the business and the way we are organised is along business lines, so it's very different from a law firm where you tend to be organised along skill sets. Within Shell we've organised with our main business units, so we have legal teams that support the downstream unit, legal teams that support the two upstream units. Shell has an upstream Americas group and an upstream international group. And we've got groups of lawyers who support them as well as the Projects and Technologies group, which is that part of Shell that implements the major projects both in upstream and downstream. There are some parts of legal that are skills based, for instance the Intellectual Property Services Group. But by and large we stay as close to the business as we can, we work out with them what their legal needs are, help anticipate some of their legal needs and support them in that way and – I am lucky – the legal team at Shell is incredibly sophisticated, incredibly knowledgeable and lots of them have been working for Shell for a long time in these areas, and they know exactly what is needed in particular circumstances.

JL: How do you decide what stays in and what goes out to private practice?

PR: Well, I suppose the simple answer to that is we keep in as much in as we can, simply because it makes more financial sense.

JL: More so than you were previously?



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PR: Shell has been doing that over the course of the last few years. My predecessor Beyard Hess had a focus on looking to make sure that we were doing as much work in house as part of an overall review of our legal costs, and certainly on the transactional side, he's been very successful in doing that. And one of the things that amazed me when I joined Shell was the huge amount of transactional work in particular that is done in house by the legal team; very high value transactions, very complex

a proper handle on the the sorts of disputes we are dealing with, where there are arguments that we need to run in certain cases, that we can run in others and also to gain learnings from that around the world and to ensure basically that we are using the outside counsel we have to use for those disputes in the most efficient and effective manner, which I am not sure at the moment is always the case.

And so that's something I am particularly focusing on. It's something I felt I could immediately bring to the business coming from the outside as I did as a dispute lawyer.

JL: You're talking about relationships not being effective, or outside counsel not always being effective. Other things that people are falling down on, for the moment?

PR: I think fundamentally on the disputes side, understanding how disputes work. Whether they are court or arbitration and being able to anticipate what is needed by outside counsel, and also at times being able properly to direct outside counsel in what you want them to do. So if you by and large are a business lawyer and occasionally have a piece of litigation or an arbitration, you are not going to have the skillset that somebody has who is dealing with it all the time. You're not going to know the process, say an ICC arbitration would run through, you're not going to know the arbitrators and the market, you are going to be entirely reliant on outside counsel. And so having people hone that side of their capabilities in house is something I want to do, so that when they are working with outside counsel there can be more of a dialogue, there can be a better strategic decision and there can also be better scoping.

I know from having been outside counsel, one of the issues you always have, one of the things you fear most is the client turning round and saying, 'you never told me that'. Now, a lot of the time clients don't necessarily want to be told that. But if you don't scope that out at the beginning and say to outside counsel, 'well actually don't worry about this area, it is a small area of risk, it's something we are prepared to take, we would like you to focus on this side of things', you can end up wasting a lot of cost and time dealing with things that you don't want outside counsel to deal with, but they feel they need to cover because of that fear of the client turning round and saying 'I never told you that'.

JL: It is early days for you at the moment, you're what, five months into the role. But in so much as you know, what are the biggest challenges facing you at the moment?

PR: The biggest challenges overall I think

'I am looking to get a more consistent approach to the way we deal with disputes around the world.'

transactions, but because they have done them a number of times already as part of their work with Shell, it is things that they can handle.

Where we need outside involvement is usually in particular areas where expertise is something we haven't got in house and in the area of disputes generally where by and large you need to have a local lawyer who is able to argue cases for you in the local courts, that is obviously something that we cannot do most of the time.

JL: You are a litigator yourself – you qualified as a QC – you are one of the few people on earth to actually do that. What impact did that have on the way Shell does things, going forward?

PR: Well, I suppose the immediate impact is I am looking to pull together and get a more consistent approach to the way in which we deal with disputes around the world. Shell, unlike most of the other major international oil companies, does not have a global litigation function at the moment.

JL: At the moment?

PR: At the moment. Because that is something I am in the process of putting in place. I recently appointed a general counsel for global litigation, and I'm using litigation in the sense of all disputes, so arbitration regulatory hearings, adjudication and so on. And we're looking to pull together within Shell a group of people who have got expertise in dispute work and have them focus together, rather more as a skillset in the way I was describing Intellectual Property Services for instance. So that when we have disputes around the world, we are dealing with them on a consistent basis and we've got

are in a number of areas. One is in the anti-bribery and corruption area. It is an area of increased focus around the world. We have got the UK Bribery Act coming out on 1 July. We have been subject to the Foreign Corrupt Practices Act for a long time because of Shell's involvement in the US, and we are, as is known, under what's called as a 'deferred prosecution agreement' with the Department of Justice as a result of a bribery and corruption issue. And that means that so far as Shell is concerned, we have to focus very hard on those issues to make sure that we have a compliant culture throughout the whole of the organisation.

One of the things I have been massively reassured by since I arrived is that culture is definitely there, it is a real focus for the CEO and all of those on the Board and on the Executive Committee, and it is something we are looking to ensure becomes part of the DNA of Shell and across all of its businesses. It is a large organisation – we operate in a larger number of countries that appear red on the Transparency International index.

JL: How many, out of interest, do you operate in on red?

PR: I don't know what the total number is, but I would certainly say a large proportion. If you actually look at their map, there is not an awful lot that is yellow, apart from North America and parts of Europe, and we are certainly in a significant number of countries in the Middle East and Africa and in the Far East, which are coloured red on that map.

JL: Okay. You pre-empted my next question on that to a degree. Shell was recently fined £48m for breaching the Foreign Corrupt Practices Act, and this was due to bribes paid to Nigerian officials, which is what the Act covers. I was just going to ask whether you learnt anything specific from that, or whether it just plays into your general point about needing to make sure that Shell is compliant across the board?

PR: Well it certainly means we need to ensure that Shell is compliant across the board. I think the specific learnings on that though are that one of the things we have to get clear within the organisation, we do a huge number of projects, a lot of the projects are schedule driven, it is important we hit our timings and so on, but there are certain things that cannot be schedule driven. And one of the things I am trying to do within the organisation is in the anti-bribery and corruption area, to get the same approach that we have successfully been able to establish in the health and safety area.

We have a thing within Shell called 'goal

zero'. We take personal safety, health and safety in particular, as well as process safety – but in the personal safety area we take it incredibly seriously, we focus on ensuring that all our people, not just the Shell employees but our contractors, work in a safe environment and that is something that is well understood. And so what I am saying to people is just as you would not, if you were behind schedule, turn round to your boss and say, 'the only way we are going to keep on schedule boss is to kill somebody,' you just would not do it and the boss certainly would not say 'do it', then you have to get the same idea so that you would feel exactly the same way and say, 'the only way to stay on schedule is to bribe somebody' and then the boss will say, 'well no, you don't do it', and you know you're not going to do it.

And so it is getting that sort of feeling right the way through the company. That yes, we need to provide delivery quickly and effectively but it has to be on the basis of certain requirements, and certainly stepping over the mark from an anti-bribery and corruption perspective is one of those that should not be driven by schedules.

JL: Clearly you have something of a challenge there to spread that across the whole of the organisation. Are there particular countries where you feel there are specific challenges?

PR: No, I think it is now well known in the organisation that – the fact that we have the DPA, as you mentioned – is well known throughout the organisation and the amount of money we had to pay as a result is also well known. I think people are now clear that this is something that is not acceptable within Shell. It never has been, but I think that has reinforced the message and the message has been reinforced right the way down from our CEO, who in his first video broadcast to the company after I joined made very clear that compliance was a real focus.

JL: Nevertheless, Shell does do business, as you say, in high risk countries and there are some countries in which it is recognised that if you do business there it is part of the culture that you are expected to pay bribes. I could name some; China, Russia – and Shell is doing business in those countries. How do you deal with that?

PR: You have to deal with it on the basis that whether it is part of the culture or not in that country, it is not part of your culture as Shell.

JL: Right.

PR: And again if you like, going back to the health and safety thing, we had an incident

recently where one of our employees was driving home, she was not feeling particularly well and she sort of had her head in her hand like that as she was driving, she was pulled over by a policeman who accused her of speaking on her mobile phone while she was driving. She did not have a mobile phone there, it just looked like it. Her immediate response was not to say 'no, I wasn't on my mobile phone', her immediate response was to say 'I work for Shell,' because at Shell you are not allowed to drive and be on your mobile phone. So in the bribery space then the same idea, whether

paid by associated persons. There, that does give a level of complexity because of the huge number of joint ventures that Shell is involved in and the huge number of contractors and suppliers we have, but again the guidance has made it clear that you need to approach that on a risk basis and that is what we are doing in terms of our due diligence with our joint venture partners, with our suppliers and so on, and we have been doing that all the time in any event. So I don't see that it's going to alter things.



you're working in China, whether you're working in Russia, or Nigeria, or wherever it happens to be, somebody asks you for a bribe, your answer should be 'I work for Shell,' and they will know you will not pay them.

JL: Despite what we said about the £48m fine, that's the obvious sort of comeback isn't it? To say, 'hang on, Shell has a track record here'.

PR: Well, track record may be putting it too high and the events that surrounded that were several years ago, albeit that the DPA was only entered into at the end of 2010.

JL: Moving on a little bit, obviously the UK Bribery Bill is coming into force. Does this add a layer of complexity or challenge for you or is it more of the same with regard to foreign corruption generally?

PR: Yes, I don't think it impacts our approach really. There are new introductions so far as what now constitutes an offence, which weren't offences under the Foreign Practices Act, so facilitation payments for instance, but Shell's code of conduct has never permitted facilitation of payments, just as we have never permitted bribery of non-government officials. So our code of conduct and the compliance regime we have in place already covers all of the areas within the Bribery Act.

One of the things that the Bribery Act has brought in is, or will be bringing on 1 July, is this strict liability corporate offence for bribes

JL: Shouldn't it, with regard to third parties? And it does seem that Shell's line of business is one where as you say you come into contact with a lot of third parties. Are there specific things you can do, or do you just have to take a risk-based approach?

PR: You take a risk-based approach in terms of the countries you're in and the joint venture partners you are operating with. Where we are in joint ventures where we are operating, or we are the dominant partner, then we always require our code of conduct to be part of the joint venture, and we are in a position to do that. Where we are not, then we always seek to ensure the regime that is fully in place meets our code of conduct and requirements, albeit that it may be phrased in a different way because the joint venture partner has a different approach or a different terminology to these things, but it is something that we always take a great deal of care about.

Certainly the defence, just to deal if you like with the other part of the Bribery Act, to that strict liability offence is that you have adequate procedures in place and we are confident that we do have adequate procedures in place – of course the guidance is relatively loose [as to] what constitutes adequate procedures. ☒



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Less power to the people in the Gulf

Decades of underinvestment in energy infrastructure, rapidly-expanding populations and the Arab Spring have left power production facilities unable to cope, meaning that nations that rank among the world's most energy-rich are facing annual power shortages that strike at the height of summer. It's a problem with no quick, or cheap, fix.

ANDREW WHITE

In 2011, life in the Gulf is played out to the incessant, tuneless drone of air conditioning units, each disgorging tonne upon tonne of chilled air to counterbalance the oppressive heat. Where once there stood windtowers designed to funnel desert air into simple stone buildings, now cold air is pumped through giant structures of glass and steel, then out into the sunshine via gleaming aluminium vents.

However, if it's a switch to which Gulf residents have become happily accustomed, it's also one which cannot be sustained. Nations which are among the most energy-rich on Earth are today facing annual power shortages that strike at the height of summer, and to which Gulf governments have no immediate solution. Decades of underinvestment in energy infrastructure, as well as rapidly-expanding populations, have left power production facilities unable to cope with demand. And what's more, one consequence of the Arab Spring which rolled across North Africa and the Middle East in the first half of 2011 is that the problem will only get worse.

Many Gulf inhabitants leave their air conditioning running around the clock, 365 days a year. In Saudi Arabia, Kuwait, Bahrain and Oman they are able to do so because the government pays heavy subsidises on electricity for nationals. And in the UAE and Qatar, locals don't need to worry about bills at all: they are totally exempt from utilities charges including power and water.

As a consequence, and despite increased government efforts to foster a culture of energy conservation, the Gulf countries' green credentials are at present plastered in dirty smudges. UAE inhabitants produce more than double the carbon emissions per capita of their counterparts in America, and close to five times that of UK residents. The UAE is joined by Qatar, Bahrain and Kuwait in a ranking of the world's top ten power consumers per capita, while Saudi Arabia and Oman make the top twenty. In Qatar, shockingly, power consumption per capita is almost double that in the UAE and ten times that in the UK.

The demand is such that the Gulf's power production facilities, ignored for so long by governments more interested in record-breaking real estate, are struggling to keep pace. In the United Arab Emirates (UAE), the northern emirates of Sharjah and Ras Al Khaimah have been particularly afflicted: in 2009 power outages forced hundreds of families from their homes in 50°C heat, and in June this year a series of blackouts hit the city of Khor Fakkan, prompting fears of a long, sweaty summer ahead. Power failures are also a frequent occurrence in the western region of Saudi Arabia, while in Kuwait last summer the country's parliament recommended cutting the working day for public sector employees, in order to conserve energy and help avoid the blackouts.

Gulf governments have realised this is a problem with no quick fix. The region's first

nuclear power stations are expected to be up and running by 2017, but in the meantime the authorities are claiming that the upgrade of existing facilities, and the provision of new production plants, will keep the lights on and the air cool. Analysts, however, are concerned: in Kuwait, for example, no new power stations have been built since 1998, and while new facilities are in the planning and construction phases, they have yet to come online. At the same time, deteriorating cabling is reported to have caused up to 80 percent of the outages experienced last summer.

It doesn't help that demand is set to soar over the coming years. Peak electricity demand in the UAE is predicted to rise by more than 12 percent annually between 2010 and 2020, according to the government's own estimates. The Kuwaiti government expects demand for electricity in the country to grow as much as seven percent annually to 2030. And in Qatar, which is preparing to host the football World Cup in 2022 and witnessed record growth in power demand among the Gulf Cooperation Council (GCC) countries in 2010, electricity consumption is expected to grow around 15 percent a year between 2010 and 2014.

By way of response, the UAE has said it will invest around \$74bn on energy projects between 2011 and 2015. According to Business Monitor International, Kuwait plans to tender an estimated \$17.4bn worth of power generation and desalination projects, while Saudi government figures have talked about spending \$88bn over the next ten years to satisfy power demand. Qatar is spending more than \$1.2bn on boosting its domestic transmission network, as part of a \$125bn spend on energy and construction projects in the run-up to the 2022 World Cup.

Qatar is in a uniquely advantageous position: although it is running to catch up with its own extraordinary growth, it does have the gas reserves to ensure long-term electricity supply. The other five Gulf states, however, enjoy no such guarantees.

'The [Gulf countries] are building gas-fired power plants, but looking forward the shortage of gas is a big problem,' says Robin Mills, an independent energy economist and author of 'The Myth of the Oil Crisis'.

'Kuwait and Dubai are already importing gas from Qatar, and while they can always get the gas they need, it's very expensive,' he continues. 'Abu Dhabi has domestic gas and plenty of big gas projects, but the projects are expensive and they are taking some time to be completed. And Saudi has just said that all its new plants will be oil-fired not gas-fired, because of the shortage, which is a very expensive solution and environmentally undesirable too.'

One potential answer to the crisis would be to slash subsidies, raising prices and thereby forcing Gulf nationals to rein in their more power-hungry practices. That option, however, has become political kryptonite in the wake of the Arab uprisings that turned the course of history over the first six months of 2011. Put bluntly, while the Arab Spring may have signified a step forward for democracy in the Middle East, it represented an inadvertent leap backward for the region's environmental aspirations, not to mention the wallets of nervous Gulf governments.

The UAE will invest \$74bn on energy projects between 2011 and 2015, Kuwait \$17.4bn. Qatar is spending over \$1.2bn on boosting its domestic transmission network, as part of a \$125bn spend on projects ahead of the 2022 World Cup.

Regimes which had previously considered slashing power subsidies, have shelved any such notions for fear of riling their citizens. Ever since the original oil boom, electricity subsidies have been seen as one way for governments to disperse oil revenues to the people, as part of an unofficial cradle-to-grave welfare system. And as the dust settles on new regimes in Tunisia and Egypt, and government forces continue to pound rebel uprisings in Syria and Libya, Gulf governments aren't about to do anything which might invite similar unrest in Riyadh or Abu Dhabi.

If locals aren't incentivised to save energy through higher prices, then the crippling demands placed on the Gulf's creaking power facilities aren't going to ease off any time soon.

Meanwhile, summer this year is shaping up to be as hot as the last. Record demand is a very real prospect, and in 2011 the Islamic holy month of Ramadan falls during August, meaning that many of the nationals who would usually repair abroad for the worst of the heat, are likely to stay at home. With the prospect of more outages looming, perhaps international investors looking for returns from the Gulf could do worse than sticking their cash into candles. ☒

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Historic justice

After graduating in 1952, Sandra Day O'Connor couldn't find a law firm willing to give her a job. Nearly 30 years later, she was the first woman appointed to the US Supreme Court, a historic milestone for women's rights. *IBA Global Insight* speaks to the former Supreme Court Justice who was at the centre of the controversial election of George W Bush.

REBECCA LOWE

Sandra Day O'Connor, sitting serenely on a pristine cream sofa in her Savoy suite overlooking London's River Thames, was just a child when she shot her first coyote. It was a tough job, she says, but somebody had to do it. 'We kept a rifle in the truck wherever we went and if we saw a coyote, I'd shoot out of the window. You were bouncing along so it was hard to do, but we needed to kill them to stop them eating our small calves.'

O'Connor has a steely twinkle in her eye as she speaks, and it is clear she enjoys recounting this tale of early grit and chutzpah. These qualities have, after all, defined the 81-year-old through much of her life and career, as

she rose from unemployed law graduate to one of the most powerful women in American history, as the first woman appointed to the US Supreme Court. In 2000, O'Connor made another indelible mark on history, playing a seminal role in arguably the most controversial Supreme Court decision when it resolved the contested *Bush v Gore* election.

O'Connor's rise to the top tier of the American judiciary came almost exactly 30 years ago, on 7 July 1981, by which time O'Connor had already served as an assistant attorney general, a state senator and an appeals judge for Arizona. Not a bad résumé. And all the more impressive considering the only job

she was offered following graduation from Stanford Law School was as a legal secretary. At the time, Tupperware parties and *I Love Lucy* – a sitcom featuring a stereotypically feeble woman, reliant on her husband – were the epitome of female entertainment.

Back at the ranch

O'Connor's unusual upbringing on an isolated ranch on the border of Arizona and New Mexico clearly played a key role in her later life and career.

Here she learnt how to 'get on and work hard', adopting those invaluable all-American traits of mettle, drive and self-sufficiency. 'You never knew from day to day what you'd have to do. In a place like that you have to fix everything to make it work. If we had to build a fence, we built it. If you had to repair your car, you repaired it. There was no one to call.'

The oldest child of three, O'Connor took on much of the responsibility for running the ranch, planning one day to take it over from her parents, just as her father had taken it over from his. Yet unlike her father, whose aspirations to study at Stanford University fell by the wayside, O'Connor left home to live with her grandmother and attend school in El Paso – and, eventually, earned the Stanford place her father had coveted.

It was here, during her undergraduate studies, that O'Connor met the 'inspirational' professor Harry Rathbun, who convinced her to stay on and take a graduate law degree. It is also here that she first encountered William Rehnquist, who went on to become Supreme Court chief justice in 1986. She and 'Bill' quickly became friends, then more than friends, as they bonded over regular games of bridge and charades at O'Connor's house: a co-op established by the widow of the former head of the education department for the small handful of graduate women who had nowhere else to live.

In 1952, O'Connor graduated near the top of her class, got married – not to Bill, but John Jay, a colleague on the *Stanford Law Review* – and excitedly entered the outside world. But the world wasn't ready for an ambitious, intelligent woman who could hold her own in conversation and shoot a jackrabbit at 50 yards. 'No one gave me a job,' she says. 'It was

very frustrating because I had done very well in both undergraduate and law school and my male classmates weren't having any problems. No one would even speak to me.'

Exhibiting the persistence and initiative for which she would later become renowned, O'Connor sought out a county attorney in San Mateo, California, who she heard had once had a woman on his staff, and agreed to work for nothing until he could pay her a salary. Four months later she was made a full employee, only leaving, reluctantly, after her husband was

drafted to the Judge Advocate General's Corps in Frankfurt, Germany, during the Korean War.

From law to legislature

When the couple returned home to Arizona in 1957, O'Connor again struggled to find work, and again used her tenacity to get herself

out of trouble by convincing another man to open a law office with her. The two primarily took on cases for people with limited funds and evidently earned a good reputation doing so, as O'Connor was soon elected a precinct committeeman by the Republican Party, and subsequently appointed to a vacancy in the Arizona State Senate. Here she was re-elected twice, and in 1973, to her 'great shock', she was made majority leader. Her surprise was perhaps understandable: it was the first time a woman in the US had ever held a legislative leadership position.

For Sandy D'Alemberte, former president of the American Bar Association, who knew O'Connor through her service as a board member of the Central European and Eurasian Law Initiative (CEELI), this tenure in the US legislature provided the justice with invaluable training for her elevation to the Supreme Court. 'She had a great ability to make people feel comfortable around her, to relate to people, and she always showed great hospitality for the people who came from other countries to visit the US,' he says. 'I think a lot of this came from her political senses.'

Mark Ellis, executive director of the IBA, who also worked with O'Connor at CEELI, has similar sentiments. 'She had an incredible ability to connect with people, which she used throughout her political and judicial career. You could tell people had this tremendous admiration and respect for her.'

'You're not going to decide some case based on your own fundamental values, which are different from everyone else's. That's not going to happen'

Justice Sandra Day O'Connor

O'Connor eventually returned to the law in 1975 as an elected county judge, and in 1979 was appointed to the Arizona Court of Appeals. Then, two years later, she suffered her next 'great shock' – when President Ronald Reagan announced he was nominating her to the US Supreme Court, following a campaign pledge to help secure the female vote. 'I had never worked at court, I had never been a law clerk there, I had never tried a case at court,' says O'Connor. 'It was far removed from our life in Arizona and I was not trying to move to

Kennedy, David Souter and Clarence Thomas, leaving White the sole 'Democratic' voice before President Bill Clinton's appointments of Ruth Bader Ginsberg and Stephen Breyer in 1993 and 1994 respectively. Liberals were crying out for moderation, and in O'Connor, it seems, they got what they were asking for.

'She didn't seem to have an overarching ideology,' says Joel Grossman, professor of political science at Johns Hopkins University and expert in US constitutional law. 'She was more conservative than not, but pragmatic

'It was one of the worst judgments the Court has ever made. The Court itself announced that it cannot be used as precedent in other cases, which is almost a concession they jumped off the rails.'

Sandy D'Alemberte, on the *Bush v Gore* decision in 2000

Washington DC. I was not sure if I went to the Supreme Court that it would be a comfortable choice for me.'

But with support from her husband ('come on, you'll be fine'), O'Connor accepted the post, and consequently carved out her own unique foothold in the history of her country. Elected to the Court by a sweeping Senate majority of 99-0 (the missing senator, Max Baucus of Montana, sent her a copy of Norman Maclean's *A River Runs Through It* as an apology for his absence), she was clearly a popular choice – even if it was due in large part to Reagan's popularity at the time.

The process, however, was far from painless. 'I was on national television every minute of every day,' she recalls. 'It was very stressful. I think I'd still be there except the wife of the committee chairman decided to have a big tea and invited everybody who was anybody in Washington to go.'

'Open and practical'

Accompanying O'Connor on the Bench were Republican nominees Rehnquist, William Brennan, Warren Burger, Harry Blackmun, Lewis Powell and John Paul Stevens, and Democratic nominees Thurgood Marshall and Byron White. Powell was O'Connor's favourite, a 'wonderful man' willing to do 'anything' she needed, whereas White – a former football halfback – had such a powerful handshake that she was forced to grab his thumb with her fist as a pre-emptive measure to prevent serious injury.

Brennan, Blackmun, Powell and Marshall were gone within the decade, replaced by Republican nominees Antonin Scalia, Anthony

really describes her. She tended to look at each case as a problem to be solved.'

'She was never doctrinaire,' adds D'Alemberte. 'She was the kind of conservative even we liberals could admire. She was always open and practical, and analysed things from some understanding of how things play out among people.'

Playing politics

Yet O'Connor's reputation as a moderate is not to underplay her essential conservatism. For the first few years, her voting record aligned heavily with Rehnquist, and between 1994 and 2004 she only joined the liberal wing of Stevens, Breyer, Ginsburg and Souter in just over a quarter of all controversial 5-4 decisions.

Indeed, perhaps the most contentious Supreme Court decision of all time was that of *Bush v Gore* in 2000, in which O'Connor played a seminal role. Voting with the 5-4 majority, O'Connor ruled that the Florida Supreme Court's method for recounting ballots was a violation of the Equal Protection Clause of the 14th Amendment and, crucially, that no alternative method could be established within the time limits set by the state. The decision gave Bush the electoral votes he needed to win the state and, consequently, the presidency.

The decision was especially contentious for O'Connor, whose husband reportedly announced to three witnesses at an election night party that she wished to retire under a Republican president. Critics leapt on this as evidence of her political partisanship and O'Connor remains prickly about the issue now. 'Look, you have volunteers working in the polls,' she says, showing her first sign of

restlessness since the interview began. 'They have to count them and they get a ballot where the chad isn't punched out. Are you going to have the same rule or just let them do anything they want? Come on. It's a federal election and you need a federal policy and you need to be able to inform the volunteers who are counting the ballots. And Florida didn't do that.'

So what about the comments blaming her decision on her plans for retirement? 'For heaven's sake, I don't care.' And did the comments have any weight? 'They were ill informed. You will always have ill-informed comments.'

Yet despite her protestations, even O'Connor's staunchest supporters have difficulty understanding the decision. 'It was once of the worst judgments the Court has ever made,' says D'Alemberte. 'It is extraordinary when you read that opinion. The Court itself announced that it cannot be used as precedent in other cases, which is almost a concession they have jumped off the rails. I can't explain why she joined that decision.'

For those outside the US, the Supreme Court's essentially partisan nature is sometimes difficult to comprehend. The idea of a committed Republican ruling on a highly politicised issue such as the election of a president seems questionable at best, unethical at worst. Yet it is a system that has endured for 222 years and looks unlikely to change in the near future. O'Connor, certainly, believes there is no need for a new one. 'I think the system's been remarkably effective: do you have a better one to propose?' she asks pointedly. I confess that I don't, but ask if she might. 'No, I wouldn't think you would. It's worked pretty well.'

Moderation in excess

It is perhaps testament to O'Connor's popularity and pragmatism that the 2000 presidential election has not marred her legacy among more liberal-minded folk as some at first believed it would. A number of other decisions seem to have mitigated the damage, including *Grutter v Bollinger*, which upheld affirmative action, and *Webster v Reproductive Health Services*, in which O'Connor refused, to Scalia's rage, to overturn *Roe v Wade*. She was also the deciding vote in several significant gender equality cases, including *Price Waterhouse v Hopkins* and *Jackson v Birmingham Board of Education* (see box).

O'Connor's opinion on abortion is perhaps indicative of her lack of judicial activism: she admits she finds abortion 'repugnant', yet has felt unable, legally, to undermine it. 'You're not

Significant Supreme Court decisions

Mississippi University for Women v Hogan (1982): O'Connor rules in favour of a male applicant seeking admission to the Mississippi University for Women nursing school.

Webster v Reproductive Health Services (1989): O'Connor votes with the majority to uphold a Missouri law that imposed restrictions on the use of state funds, facilities and employees in performing abortions, but refuses to overturn *Roe v Wade*.

Price Waterhouse v Hopkins (1989): O'Connor holds with the majority that Price Waterhouse failed to prove by a preponderance of the evidence that its decision not to promote a female employee would have been the same if sex discrimination had not occurred.

Missouri v Jenkins (1995): O'Connor votes with the majority in a 5-4 ruling to overturn a district court ruling that required the state of Missouri to correct racial inequality in schools by funding salary increases and remedial education programmes.

Davis v Monroe County Board of Education (1999): O'Connor writes for the 5-4 majority that a school can be held responsible under Title IX of the Education Amendments of 1972 for 'student-on-student' sexual harassment.

Boy Scouts of America v Dale (2000): O'Connor joins the majority in a 5-4 decision holding that New Jersey violated the Boy Scouts' freedom of association by prohibiting it from discriminating against its troop leaders on the basis of sexual orientation.

Bush v Gore (2000): O'Connor provides the deciding vote in a ruling that stops the Florida election re-count and effectively gives the presidency to George W Bush.

McConnell v FEC (2003): O'Connell provides the deciding vote in a judgment that upholds the constitutionality of most of the McCain-Feingold campaign financing bill regulating 'soft money' contributions.

Grutter v Bollinger (2003): O'Connor authors the 5-4 majority ruling, which upholds the affirmative action admissions policy of the University of Michigan Law School.

Lawrence v Texas (2003): O'Connor writes a concurring opinion stating that state laws prohibiting homosexual but not heterosexual sodomy violate the Equal Protection Clause of the 14th Amendment.

Jackson v Board of Education (2005): O'Connor writes for the 5-4 majority that retaliation against individuals because they complain of sex discrimination is intentional conduct that violates the terms of Title IX of the Education Amendments of 1972.



‘She didn’t seem to have an overarching ideology... She was more conservative than not, but pragmatic really describes her. She tended to look at each case as a problem to be solved.’

Joel Grossman
Johns Hopkins University

going to decide some case based on your own fundamental values, which are different from everyone else’s,’ she says. ‘That’s not going to happen.’

Interestingly, considering her legacy as a champion of women’s rights, O’Connor’s dismissal of value-judgments extends to her view of gender roles. Her appointment, she feels, was positive in the inspiration it provided for other women to escape a world of pinafores and petticoats; yet she does not feel that she, as a woman, brought anything fundamentally different to the Court and even resents the label ‘feminist’. ‘At the end of the day, you have to resolve something on legal principles and you’re not going to do something different just because you’re a man or a woman.’

Since stepping down in 2006, O’Connor’s absence on the Court has been mourned by many, who are discomforted by its ideological shift to the right. The retired justice herself at first refused to be drawn on the subject, but has since become more outspoken. ‘What would you feel?’ she said at a May 2009 panel discussion at the College of William and Mary, Virginia, where she is Chancellor, when asked how she felt about the Court’s retreat on some of her judgments on abortion rights and campaign finance. ‘I’d be a little bit disappointed. If you think you’ve been helpful and then it’s dismantled, you think: “Oh dear.” But life goes on. It’s not always positive.’

Enduring legacy

Life does, indeed, go on. Since leaving the Court in 2006 to care for her husband, who suffered from Alzheimer’s for many years and died in 2009, O’Connor has hardly been your conventional octogenarian grandmother. Alongside raising awareness for Alzheimer’s research, she has led a campaign against the election of judges (‘I can’t imagine why we

do it’) and denounced Republican attacks on judicial independence after a series of public criticisms of court decisions (‘It takes a lot of degeneration before a country falls into dictatorship, but we should avoid these ends by avoiding these beginnings’).

After despairing that only a third of young people could name the three branches of government, O’Connor also set up an interactive website, www.ourcourts.org to be used in schools as a civic educational tool, which has since proved a great success.

But despite all these achievements, will history remember the ranch-girl-made-good as anything other than a timely symbol of female emancipation? For many, the answer is yes; her flexible approach, they say, had greater impact on legal precedent than that of the more intransigent ideologues on the Supreme Court. Others, however, question whether she has quite made the cut. ‘The great justices are the ones who write the opinions that we teach in constitutional law, and, other than a few cases, hers were not quite at that level,’ says Grossman. ‘She left her mark, but it’s not a mark that will be remembered in 200 years.’

History, it is true, often has trouble remembering moderation, subtlety and restraint when faced with the more virile alternatives of passion, ambition and energetic zeal. Yet it is clear that O’Connor had all these things, lacking ideological ardour, but zealous in her pursuit of social justice and equality. Whether she herself wishes, or expects, to be remembered by posterity for her good works, she, with characteristic modesty, declines to say. But, she is clear on what she would like on her tombstone. ‘It was what I told Congress when they were interviewing me,’ she says. “‘Here lies a good judge.’” ☼

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The struggle for Africa

While the Democratic Republic of Congo is among the world's most resource-rich countries, it has also been crippled by war and corruption. *IBA Global Insight* assesses the ongoing fight to establish law and justice in the heart of Africa.

RUTH COLLINS

In June last year, the Democratic Republic of Congo (DRC) celebrated 50 years of independence from Belgium. Despite the festivities, the country had little to celebrate. The DRC has been characterised by brutality for over a decade and an estimated 5.4 million people have died from the effects of the country's two recent wars. Although the 2006 election – the country's first free elections for four decades – suggested progress, the country has seen the rape of more than 200,000 women and children over the past 12 years. The eastern provinces of North Kivu and South Kivu, which share a border with Rwanda, have been two of the areas most affected by violence, displacement and insecurity due to continuous clashes between rebel groups, pro-government militia and the armed forces.

Father Justin Nkunzi, director of the Justice

and Peace Commission of Bukavu and partner of UK-based NGO CAFOD, highlights the exploitation of mineral resources such as coltan, cassiterite and wolframite as a key vehicle fuelling the conflict. These metals are used in the manufacture of mobile phones and laptops all over the world. 'Rape for minerals in these communities is used to humiliate, kill and consequently transmit Aids,' says Father Nkunzi. 'By attacking women, not only are these men attacking our families but also our society and African culture itself. I'm sad to say that sexual violence is killing Africa and mutilating a part of our humanity.' In October 2007, UN Under-Secretary-General John Holmes described the problem of sexual violence in the DRC as the 'worst in the world'. In a joint statement to mark the country's anniversary, Congolese bishops wrote that 'the DRC has

moved backwards rather than forwards.’ However, against the odds, new regulations and a rise in convictions of army officials may point to a brighter, more promising future for Congolese citizens.

Bukavu

Bukavu, the unassuming capital of the DRC’s South Kivu province, has been a scene of rape, pillage and destruction countless times over the last 15 years. In August 1998, the Congolese Rally of Democracy (RCD) captured the city and civilians became embroiled in a war between Tutsi government forces and the Democratic Liberation Forces of Rwanda (FDLR), which comprises mainly Hutus who fled Rwanda following the Rwandan Genocide in 1994. In June 2004, in an alleged move to protect Congolese Tutsis from genocide, Congolese rebel General Laurent Nkunda unleashed his rebel forces, the National Congress for the Defence of the People (CNDP) upon Bukavu. The fighting exacerbated tensions and violence in the South Kivu province and Congolese citizens took to the streets to protest against the UN’s failure to protect the city from General Nkunda’s forces.

Bukavu is also home to the Panzi Hospital, which provides vital medical assistance to victims of the conflict. The hospital’s founder and leading gynaecologist Dr Denis Mukwege was awarded the UN Human Rights Prize in 2008 for his treatment of thousands of women who have been severely mutilated and traumatised by soldiers in the region. According to official UN figures, more than 5,000 women were raped in South Kivu alone during 2009 – the majority were raped by soldiers or armed rebels. From its foundation in 1999 to June 2010, the hospital treated 25,441 victims of sexual violence and genital mutilation.

Despite the ongoing conflict, the Panzi Hospital is still a beacon of light for the country’s women and children. Yet the task of ‘detransforming the community,’ as Father Nkunzi puts it, is a formidable one. He laments the way in which rape has permeated the country’s culture and stigmatised his people’s identity: ‘I have even heard people say that rape was part of our culture. As a Congolese, I feel personally frustrated and I am ashamed to say I am a man. Instead of protecting life here, other men are destroying it.’

The role of the UN

MONUSCO, the official title of the UN peacekeeping force in the DRC, is currently the largest peacekeeping operation in the world, with more than 20,000 blue helmets deployed

in the area. It costs an estimated US\$1.35bn a year, but there is rising scepticism over its role and effectiveness in the country. In 2000, the rising violence in the country pressurised the UN Security Council into passing Resolution 1325, which advocates the full participation of women in conflict resolution and peace building processes. In 2008, further pressure caused the UN to pass Resolution 1820, which orders all armed forces to put an end to using sexual violence as a means to humiliate and intimidate civilians. To date, neither resolution has been fulfilled.

However, MONUSCO has made some important progress in the region. The beginning of 2009 saw the launch of an unprecedented joint military operation between Rwanda and the DRC against

‘Anvil’s material support enabled the Congolese army to reach the remote town of Kilwa at top speed – where they then carried out widespread abuses against the civilian population’

Tricia Feeney
Director of Oxford-based RAID

Rwandan Hutu rebels in North and South Kivu. However, although they succeeded in capturing General Nkunda, the resurgence of Bosco Ntaganda, renegade military chief of the CNDP, and the continuing presence of other rebel groups in the region indicate that the roots of the conflict are far from waning. Many Congolese condemn MONUSCO for turning a blind eye to war crimes.

In May 2009, President Joseph Kabila passed a law granting amnesty to militias in the east of the country for conflict-related violence committed since 2003. Although the law did not offer amnesty to those accused of war crimes, many Congolese believe that the amnesty simply acted as a means of further perpetuating the cycle of impunity. The amnesty itself indicates that there is still a long way to go for women’s rights and indeed human rights in the DRC and that even the largest UN peacekeeping mission in the world is inadequate for a country the size of the whole of Western Europe.

MONUSCO came under fire in October 2008 when it failed to prevent the violent CNDP offensive that killed and displaced hundreds. MONUSCO has been strongly criticised by human rights groups for its failure to reprimand Bosco Ntaganda, who is

wanted in the ICC for allegedly conscripting and sending children under the age of 15 to fight. In July 2010, between 200 and 400 rebels raped and looted the town of Luvungi and five other villages, only ten miles from a UN peacekeepers' base. Nearly 200 women and four baby boys were raped in the attack and human rights groups bitterly condemned the UN for failing to protect Congolese citizens. The Congolese Government has requested UN forces to withdraw before September 2011.

An end to impunity

Inadequacies and obstacles in the DRC's own judicial system have also played a large role in perpetuating the country's conflict-related violence. In 2007, Global Witness, Rights and Accountability in Development (RAID) and two Congolese NGOs, published a report entitled *The Kilwa Trial: a denial of justice*. The report highlights serious failures and irregularities in the six-month long trial against extrajudicial killings, torture, rape and looting carried out by the Congolese Armed Forces (FARDC) in October 2004 in the town of Kilwa, which is located in the Katanga province. The trial ended on 28 June 2007, with the defendants acquitted of all charges.

Marie-Pierre Olivier, a senior programme lawyer at the International Bar Association's Human Rights Institute (IBAHRI), was part of a six-person delegation consisting of members from the International Legal Assistance Consortium (ILAC) and the IBAHRI, which visited Kinshasa, Kisangani and Lubumbashi in February 2009. The delegation published a report of its findings entitled *Rebuilding courts and trust: An assessment of the needs of the justice system in the Democratic Republic of Congo*. The report identifies key issues such as a lack of funding as a fundamental setback to the Congolese justice system. 'The report also highlighted the problem of impunity in the armed forces and the consequences of "brassage", whereby members of the various militias were integrated in the FARDC without a thorough vetting process,' comments Olivier. She draws attention to the high volume of sexual and violent crimes committed by members of the armed forces and stresses that 'those responsible must be held accountable and commanders who have ordered such acts, or failed to punish them, must also be prosecuted'.

Although the Kilwa trial had seemingly collapsed in 2007, in November 2010 the Canadian Association against Impunity (CAAI) brought the case back to global attention when it filed a class action against Canadian company Anvil Mining for alleged complicity in the

Kilwa incident, which killed over 70 Congolese citizens. The group claims that Anvil provided transport, drivers and logistical support to FARDC to help them take over Kilwa. 'Anvil's material support enabled the Congolese army to reach the remote town of Kilwa at top speed – where they then carried out widespread abuses against the civilian population,' commented Tricia Feeney, Director of Oxford-based RAID. CAAI's move to bring actions against the company in a Montreal Court highlights not only the severity of the obstacles facing the justice system in the DRC, but also that foreign NGOs are now prepared to take action to prosecute companies that commit human rights violations.

In the DRC itself, it is also clear that considerable progress has been made. In February 2011, a DRC national army commander, Lt Col Kibibi Mutware, was sentenced to prison for 20 years for crimes against humanity. He was convicted of instructing his troops to rape, beat and loot citizens in Fizi on New Year's Day. Three officers and five soldiers serving under Lt Col Mutware were also sentenced to 20 years and between 10 and 15 years respectively. This is the first time in the DRC's history that a high-ranking commander and other members of the armed forces have been arrested, tried and convicted for sexual violence and related atrocities.

In early March, 11 army officers were convicted of conflict-related violence in Katasomwa, in South Kivu province in September 2009. This included Lt Col Balumisa, Major Elia and Captain Mukanyaka Kirungu Kilalo. The eight soldiers remain on the run but were sentenced to life imprisonment. Later that month, 16 soldiers and policemen were convicted of sexual violence and armed robbery in the Bukavu region. At the end of March, General Kakwavu was charged with raping two women. He is the first general to be prosecuted before a military tribunal for rape. Judicial proceedings have also been initiated for two other high-ranking officers. MONUSCO provided logistical and material support for all of these trials.

'These actions send a powerful signal that no military or political leader is above the law, and no woman is below it,' commented Margot Wallström, the Special Representative of the Secretary-General on Sexual Violence in Conflict, in a statement. 'It also shows that the focus on ending impunity for this type of crimes continues to render concrete results,' she added.

'The decisions also show the success of mobile courts, which bring justice closer to the people and closer to the victims,' comments Olivier. In the DRC, mobile courts are currently being funded by international donors. Olivier

hopes that the recent successes will show the DRC Government that it should invest money in these courts to help integrate them into the justice system and mitigate future injustices.

In February this year, the IBAHRI and the Lubumbashi Bar presented a workshop on international criminal law in Lubumbashi. The event was attended by over 100 lawyers. Olivier highlights the importance of such training opportunities for the legal community in the DRC: 'Lawyers are often forgotten in training sessions organised by donors, who [tend to] focus on judges, but lawyers play an important role in bringing cases, new arguments and making jurisprudence evolve,' she comments. 'Sensitising lawyers to the role they can play in the fight against corruption can only help the justice system become more transparent and effective.'

Conflict resolution

The last few months have also seen some considerable developments in corporate social responsibility initiatives affecting the DRC. On 24 March 2011, John Ruggie, the UN Special Representative for business and human rights issued the highly-anticipated *Guiding Principles on Business and Human Rights*. The report proposes new global standards with which businesses must comply in order to protect human rights of employees and their local communities and protect the surrounding environment.

The report's *Protect, Respect and Remedy* framework specifically targets the issue of supply chains in high risk environments such as the DRC and outlines plans to put both judicial and non-judicial grievance mechanisms in place. 'The international community has become increasingly concerned with large-scale impact of businesses in the mining industry, the oil industry, and the operation of sweatshops, so the UN has set out to develop a consensus around viable rules for better corporate practices,' commented Ruggie in a press conference. Although pressure groups such as Human Rights Watch have already described the new guidelines as 'inadequate', nevertheless they were adopted by the UN's Human Rights Council in June 2011.

Furthermore, at the beginning of April, the Global e-Sustainability Initiative (GeSI) and Electronic Industry Citizenship Coalition (EICC) launched a Conflict-Free Smelter Program to stop the sales of minerals used in electronics from funding wars across Central Africa. The Program was developed in response to the conflict minerals provisions of the Dodd-Frank Wall Street Reform and Consumer

Protection Act of 2010. It is backed by high-profile companies such as Apple Inc and Intel Corp and will require any company subject to US regulations to disclose the source of gold, coltan, tungsten and tin ore supplies and confirm that the purchases are not funding armed groups in the DRC.

However, there are concerns that a number of companies may be forced to divert their interest elsewhere if they cannot satisfy the new regulations in time. This

'No military or political leader is above the law, and no woman is below it'

Margot Wallström
Special Representative of the Secretary-General
on Sexual Violence in Conflict

could be a major blow to the DRC, since around 60 per cent of its income is based on mining activities. A mining ban imposed by President Kabila was lifted in March over concerns of its detrimental impact on the local economy and concerns that it had led to a rise in looting of the region's minerals by police, soldiers and rebel groups. President Kabila had imposed the ban in September in an effort to root out so-called mafia groups that dominate the mineral trade in the DRC. However, the DRC Government claimed that the ban had helped them identify and remove a number of these groups. In February, the country's mining minister Martin Kabwelulu announced that the government was already working with international partners to develop ways of tracing the supply chain of its minerals.

In spite of the ongoing conflict in the DRC, it is clear that the country is moving in the right direction. It is doubtful whether the Conflict-Free Smelter Program can ensure complete transparency across the supply chain. Nonetheless, it signals a positive step in that companies will finally be forced to take responsibility for their actions. Equally, the number of army officials who have been convicted of conflict-related violence over the past few months indicates that the DRC Government and international bodies are making some real progress in bringing justice to the DRC. None of these changes will succeed in eradicating the country's problems overnight, but they are certainly a step forward. ☒

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Continent at a crossroads

The complete 'recalibration of the world economy' and Africa's growing trade with emerging partners such as China, Korea, Brazil and Turkey means there's been no better time for Africa to develop. But it must focus strategically or risk a return to the past.

KAREN MACGREGOR

Africa stands at an economic crossroads. The high road builds on a decade of growth and investment in infrastructure and development to see the 'continent finally emerge as a serious player in the global political economy, with more diverse, sustainable economies and greater prosperity for its people. The low road sees political and social upheavals impede growth, trade opportunities wasted and economic bounty squandered, entrenching historic problems. But not for half a century have Africa's prospects been better.

What will be crucial, if Africa is to transform robust growth into permanent gains, will be a continental regulatory framework for engaging with economic powers, country collaboration in blocs that benefit from joint global clout, smart strategies and negotiation with emerging and traditional trade and aid partners, reduced trade barriers, pro-growth policies and investing economic gains in key infrastructure and in inclusive socio-economic development.

In June the 2011 African Economic Outlook was published, the tenth edition of the respected annual publication of the African Development Bank (AfDB), OECD Development Centre, United Nations Development Programme and United Nations Economic Commission for Africa. It describes a decade-long trend of improved economic growth and performance, and reports that Africa's economies have weathered the global crisis quite well.

While high food prices and unrest in North Africa will slow the continent's average growth rate from 4.9 per cent in 2010 to a likely 3.7 per cent this year, Outlook predicts that growth will accelerate to 5.8 per cent in 2012 – higher than in Europe and the Americas but lagging behind Asia – unless interrupted by global economic factors or deteriorating situations in Libya and Côte d'Ivoire, or more recently drought and starvation affecting millions in the Horn of Africa.

Outlook argues that the world can no longer be divided between North and South, rich and poor. It develops former World Bank President

James Wolfensohn's concept of a four-speed world of 'affluent', 'converging', 'struggling' and 'poor' nations based on income and growth rates. This 'reveals a new global growth map: some developing countries are beginning to catch up with the living standards of the affluent, others are struggling to break through a middle-income 'glass ceiling', while some just cannot shrug off the weight of extreme poverty.'

Two distinct time periods emerge, the report says. The 1990s was another lost decade for most developing economies, hampered by financial crises and instability. But in the 2000s, much of the developing world enjoyed its first strong growth in years. 'The new millennium saw Africa's per capita incomes rise faster than high-income countries for the first time since the 1970s. The number of converging countries – those doubling the average per capita growth of high-income OECD nations – rose from 12 to 65. The number of poor countries fell from 55 to 25,' according to Outlook.

'In Africa, while a group of poor countries – mostly in west and central Africa – continued to underperform, it is striking that 19 countries made it to the converging category in the 2000s, compared with only two in the 1990s.' While most converging countries are struggling to contain poverty and inequality, there has been 'a dramatic change in Africa's average growth performance compared with the rest of the world'.

The report finds that despite growing wealth, Africa is battling to reduce poverty, for three main reasons: there has only been high growth for a decade, it has not been high enough in sectors that involve the poor, and inequalities linger with growth benefiting a small part of the population. But while Africa has the lowest Human Development Index (HDI) score of any region, in the past decade all countries except Zimbabwe improved their HDI score and Sub-Saharan Africa made rapid progress, with regional HDI rising by 23 per cent.

There have been considerable improvements in macro-economic management and in political governance, although Freedom House

still classifies 20 of Africa's 54 countries as 'not free'. Outlook reports that while last year saw intensified civil protests, government responses in the form of violence and restrictive political measures continued to follow a downward trend 'and were much less aggressive than in 2008'. Last year 13 countries held largely peaceful elections, and this year there will be a record 28 national elections.

The report looks in depth at Africa and its emerging partners, which it says are 'a key part of the recalibration of the world economy'. In the past decade, Africa's trade volumes with its emerging partners have doubled in nominal value. In 2009, China overtook the US to become Africa's main trading partner, while the share of trade conducted by Africa with emerging partners – especially China, India, Korea, Brazil and Turkey – has grown from 23 per cent to 39 per cent in the last ten years.

Traditional partners still account for the largest proportion of Africa's trade (62 per cent), investment (80 per cent) and official development assistance (90 per cent), but Outlook points out that 'emerging economies can provide additional know-how, technology and development experiences required to raise the standard of living for millions of people on the continent'.

Africa is gaining from growth of world trade, high commodity prices and rising export volumes, Outlook says. Services trade also increased, highlighting Africa's growing potential and prospects in services sub-sectors. But high food and oil prices are restraining the income of African consumers, and oil- and mineral-rich countries have benefited disproportionately.

Since 2000 the amount of foreign direct investment (FDI), portfolio investment and official development assistance to Africa has increased almost five-fold, from US\$27 billion to US\$126 billion, and FDI amounted to one-fifth of Africa's gross fixed capital formation. Importantly, since 2005 Africa has attracted more investment than aid, and its share of global FDI flows has risen from 0.7 per cent in 2000 to 4.5 per cent in 2010.

'These figures offer an impressive testimony to Africa's changing role in the world and its increasing ability to harness opportunities from globalisation,' Outlook says. Of course, there are enormous challenges. One is (especially youth) unemployment, which increases risks of social unrest. Another is over-dependence on unprocessed raw materials. There are also weaknesses in governance, infrastructure, policies and human resources. But the evidence points to steady, if slow, progress in many of these areas.

Outlook proposes a continental regulatory framework for engaging with economic powers,

probably at African Union level, in consultation with the private sector and civil society. 'Africa-wide attempts should be made to coordinate trade preference regimes with traditional and emerging partners. This would enable Africa to conduct streamlined trade with the rest of the world at a lower cost.'

It recommends that African countries develop closer cross-border ties in dealing with partners and bigger markets, and make further progress towards regional coordination and integration—to improve their bargaining power. Defining national development priorities will be key to reaping benefits from growth, as will unleashing the potential of the private sector. The report identifies regional infrastructure development as crucial, as well as coherent activities covering energy, transport and communications, and says progress requires 'a leap forward in the quality of policy-making and governance'.

In 2009, China overtook the US to become Africa's main trading partner, while the share of trade conducted by Africa with emerging partners has grown from 23 per cent to 39 per cent in the last ten years.

Diana Games, Vice-President of The Africa Advisors at Global Pacific & Partners, argued in South Africa's Business Day that African countries need to manage their growing bounty to invest in the future, not squander it on recurrent and unproductive expenditure. In the flush of success and investor attention, governments should 'not take their foot off the reform pedal' and must make sure new investment actually makes a difference:

'The diversity and increasing scale of trade with and investment into the continent means that there will never be a better time for African countries to develop their economies. If they do not focus more strategically now, in 20 years' time Africa may be back where it started at the beginning of this boom era.' ☒

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The risks of the Middle Kingdom

IBA Global Insight assesses the issues facing foreign investors venturing outside Beijing or Shanghai.

PHIL TAYLOR

We've all heard the China Miracle hyperbole: unstoppable growth, huge untapped potential, an incubator for millionaires. Most of us have probably heard the doom and gloom about the country's hinterland, too – the stories of stolen IP, tales of rampant corruption, and predictions of impending burst-bubbles. It can be hard to know what to believe, and on closer inspection it seems there is truth in both sides of the story. There's no denying that there are still plenty of opportunities to make money in China. But it's also clear that China's investment landscape is changing.

Although they still have further to go, China's first-tier cities (Beijing, Shanghai, Guangzhou and Shenzhen) are now well-developed bastions of capitalism – albeit with a very strong socialist flavour. For those cities, to quote Churchill, 'it is, perhaps, the end of the beginning'. Foreign money is increasingly flowing further inland as smart investors follow the lead of the Chinese Government's Go West programme. (Although it was originally intended to last ten years, the plan, which was launched in 2000, appears to have been given a new lease of life with a new injection of capital into the country's western areas in July 2010.)

China's so-called second- and third-tier cities (see sidebar *Life in the provinces*, p39) offer many benefits when compared with Beijing and Shanghai. The most obvious is financial: there is a

large potential market and labour, rent and essential services are cheaper. Rail and air transport links to the financial and political capitals have improved vastly in recent years, and some cities offer international direct flights (Hangzhou, for instance). Shanghai-based Freshfields Bruckhaus Deringer partner Alan Wang says that although lots of tax advantages have been removed since 2008, there are still plenty of incentives available to foreign investors, including cheaper land and government grants and subsidies. This is particularly true in so-called encouraged sectors (such as healthcare, biotech, renewable energy and agriculture technology).

Another apparent advantage to China's smaller cities is competition, or, more accurately, a relative lack of it.

'Depending on your industry, second- or third-tier cities are much less crowded markets and can be easier to penetrate,' says Ronan Diot, chair of the legal working group of the European Union Chamber of Commerce in China.

Horror stories

In the real world, of course, every silver lining has a cloud. As in any country, investing in a less-developed area has its drawbacks and risks, and China can sometimes yield up stories that are hard to believe. On the popular *China Law Blog* Harris & Moure partner Dan Harris writes that he has, like all lawyers who work with China, 'a ready set of horror stories, which I rotate depending on the occasion'. He goes on to mention gems including, 'The guy who "invested" US\$500,000 into a China business



because the owner of the Chinese business was allegedly the son of a five-star general' and 'The guy who bought a million-dollar condo in Shanghai in the name of his girlfriend because he believed foreigners were not allowed to own real property in China'.

Or take a more sensational example given by Violet Ho, a managing director at Kroll and head of the global risk consultancy's Beijing office.

'We were asked to do some seller's diligence

for a US client who was approached by a Chinese entrepreneur who said he was interested in buying a lot of shares and holding a board position,' she tells *IBA Global Insight*. 'Our initial mandate was to find out whether this person really had money. Yes, he had a lot of money, but where he got it was a different story. We found out that the person was one

of the kingpins of an organised crime syndicate in a third-tier city. There were reports of how he chased after people who owed him debts by cutting off people's fingers.'

Further investigations by Kroll revealed that the potential buyer's brother was on a most wanted fugitive list for a violent crime. And he was still an active board member of one of the potential buyer's companies.

What seems to amaze Ho more than the story itself is the client's reaction.

'It felt like we were having parallel conversations; their consideration was, "are we going to get paid?" They felt that because their operation was in the US, they would have control of the management and this person would always rely on them to run the business,' she says.

Ho makes it clear that this is an extraordinary

case: 'We don't deal with criminals every day,' she says. But the story neatly illustrates that one of the real risks of doing business in China is the suspension of disbelief. Many experienced advisers will tell of how foreign investors seem to leave their common sense at the front door when looking to build their China portfolios: a modern-day Gold Rush mentality.

'The problem is there's so much information about China, it can be hard to work out what

you really need to know. Also, it's such a huge potential market – executives get very excited and maybe then forget some basics,' says Neal Beatty, regional director of global client services for Greater China at Control Risks.

One of these 'basics' is following the local law; there are some foreign investors who have, so far, managed to gain prosperity in

China without doing even that, building a false sense of security for those who come later.

'Too many foreign companies have run afoul of the local rules and it is a really bad idea to think that it's OK because "most companies are doing it" or "there is no other way". This is simply not true,' says Diot.

Getting away with it

Outside Beijing and Shanghai, there is a complex network of provincial and city-level regulations overlaid on the national law. These are often quite opaque, with little information available in English. A lack of strict filing requirements means it is difficult to get up-to-date information on private companies. It is also more common

'Oftentimes, the smaller cities will allow foreign companies to bypass certain laws in an effort to get the foreign company into their town as quickly as possible'

Dan Harris
Harris & Moure



to encounter unscrupulous auditors and local officials who will turn a blind eye. Here we see another real risk coming to the surface: it can often be much easier to get away with things in smaller cities that would be impossible in somewhere like Shanghai, and this can lead to a false sense of security.

‘Oftentimes, the smaller cities will allow foreign companies to bypass certain laws in an effort to get the foreign company into their town as quickly as possible,’ explains Harris, speaking by phone from Beijing. ‘The foreign company goes along with the shortcut, figuring it must be OK if the city itself is signing off on it. This can be a big mistake as it is exactly these sorts of cities that tend to be subject to audits at the provincial or maybe even the national level.’

Harris mentions by way of example two foreign companies that were formed in very small cities, even though they had not satisfied all the requirements for forming a wholly foreign-owned enterprise (WFOE). They ended up being shut down within a year due to audits that came down from the central government.

‘This is a very real risk that businesses are simply missing,’ says Harris.

Don't get carried away

Another risk arises from a misinterpretation of one of the key concepts in Chinese society: ‘guanxi’. The word essentially describes the key ingredient in personal relationships of influence in Chinese society – a kind of who-you-know networking concept – and there is no denying that creating and maintaining good relationships with regulators and local officials can be a very important element of business success.

‘Guanxi is absolutely a good thing. Government endorsement and support is very good to have and can ensure the long-term prosperity of a company,’ Ho says. ‘But people don’t pay enough attention to dissecting it. Not all guanxi is created equal.’

She divides guanxi into several types. Inherited guanxi is exemplified by the influence of government officials’ offspring (known as princelings). This type is often very dangerous as it is susceptible to political volatility. Personal guanxi – where a company relies on one person for its success – can be very risky, particularly where little is known about

‘One of the real risks of doing business in China is the suspension of disbelief’

Violet Ho
Kroll

that person. A foreign business that falsely believes a connection with a single influential political figure will keep it out of trouble can quickly find itself operating in a legal grey area.

‘Many people can tell you of their formerly rich and successful friend who is now serving 16 years for bribery and embezzling company property,’ says Diot. ‘Generally speaking, it is often a strategic mistake to rely on one well-connected individual for the development of one’s business in China.’

A powerful local figure can also become a liability when they start to use their connections to override a contract or exert influence on a local judge. For these reasons, a foreign company may go too far in its attempts to nurture what it perceives as an important relationship. Lavish gifts or extra cash payments make a company easy prey for extraterritorial anti-corruption laws such as the US Foreign Corrupt Practices Act, the OECD Anti-bribery Convention, or the UK’s new Bribery Act.

‘In addition to purely legal aspects, our advice to clients is to take their home jurisdiction as guidance: if you would not feel comfortable

doing what you plan to do in China back home, then do not do it,' says Diot.

Harris is more direct: 'Making good connections makes sense but running afoul of anti-bribery legislation does not. Know what the laws are and do not violate them, no matter what.'

A more positive type of *guanxi* is what Ho calls institutional *guanxi* – support from a particular government agency – which she says should be carefully developed. She also describes 'a new generation of *guanxi*' whereby a company receives strong government support because it is considered a leading enterprise in the local area.

'An enterprise that has contributed to local development, paid a lot of taxes, and employed a lot of local people can find itself in a win-win situation where it is being recognised and supported by the government for its contribution,' says Ho.

The conclusion is straightforward: *guanxi* should be about networking and making connections, and not much more. It should be used as it would in the West – to get to know the right people. This might in turn improve the chances of winning some business. It should never be seen as a long-term solution because it is by nature about personal relationships. It can never be permanent and is always susceptible to political or institutional change. Furthermore, many foreign companies (and Chinese businesspeople) probably do not possess the amount of *guanxi* that they claim to have. And even if they have enough to push through a deal, such as the formation of a WFOE, by bypassing the law, the gains will only be short term and the potential for disaster is high.

'I've had two grown men break down in tears in front of me, because they spent five years setting up their company but they didn't take the time to do it properly, and once they started making money they got booted out by their Chinese partner,' says Harris.

Reasons and motives

As we saw earlier, the main reasons behind moving to a smaller Chinese city are, broadly, low cost, high market potential and lack of competition. But these three factors are not always present, or can be over-stated. For example, some foreign companies may nowadays find the retail sector in Shanghai and Beijing too intensely competitive and so make a move to a city such as Qingdao, only to find there is no market there at all. Or company bosses can sometimes become so intoxicated with what they see as the cost benefits of relocating inland that they fail to

think through all the implications. Kent Kedl, Control Risks' managing director for Greater China and North Asia, says that this mirrors what happened 20 years ago: then, American companies became very excited by the fact that Chinese factory workers were about 30 per cent cheaper than those in the US, and failed to take into account the efficiency and infrastructure issues that would also have to be overcome.

'I think we're in danger of making the same mistake this time; we didn't learn the lessons, and people are just blindly looking West,' he says.

'There are lots of times where second- and third-tier cities are definitely the way to go; but don't just jump in because there are also many things about those cities that can make them more difficult,' adds Harris.

Some provincial Chinese cities are grappling with infrastructure issues, low water quality and power brownouts and blackouts. According to China's *Xinhua* news agency, the government of Zhejiang province (home to Hangzhou city, a manufacturing centre and logistics hub) is predicting a power shortfall of between 3.5 million and 5 million kilowatts this summer. Beatty says one of Control Risks' clients in the southwest of China has experienced big issues with its gas supply despite operating its manufacturing facility in a relatively new industrial zone.

Intellectual property is another area of potential difficulty. Although the risk of IP theft itself may not be any higher in the provinces, the difficulty of dealing with the aftermath is usually greater. Take the case of a foreign company that agrees to license its IP to a Chinese company for a year. If the Chinese company keeps on using the IP, the chances of being able to stop the company will be greater in Shanghai than in a smaller city like Chengdu. A risk factor like this, although hard to quantify, should influence a foreign company's decision regarding where to locate. Harris talks of a software company that wanted to set up in Chengdu and employ five people to write software there. It turned out that this would only have saved the company about US\$25,000 a year.

'If they were making widgets, then I wouldn't have raised the issue with them, but is it worth it for the IP risk?' asks Harris.

Local know-how

If, after carefully considering the pros and cons, a foreign investor should decide to go into one of China's smaller cities, it will be important to have local expertise alongside to help navigate

Life in the provinces

Key facts on China's so-called second- and third-tier cities:



Chengdu, Sichuan province

Population: 11 million

A national electronics and IT hub; host to many foreign hi-tech companies including Intel, Cisco, Sony, Toyota, Motorola, Ericsson, Microsoft and IBM; and an important financial hub for western China.



Chongqing

Population: 31.4 million

One of four directly-controlled municipalities in China. A largely industrial city, one of the country's largest motor vehicle production centres, and a key Yangtze River port. There was a significant clampdown on organised crime in the city in 2009, following several years of notoriety.



Nanjing, Jiangsu province

Population: 8 million

A former capital city and known as a business centre; economy built on five pillars of electronics, cars, petrochemical, iron and steel, and power. Home to several large state-owned firms as well as foreign corporations including Volkswagen Group, Iveco and Sharp.



Qingdao, Shandong province

Population: 7.5 million

Known for its brewery; also home to large Chinese companies such as Haier and Hisense. The city has a reputation for its good quality of life, which makes it relatively popular with expats.



Wuhan, Hubei province

Population: 9.1 million

Home to a large number of French companies, and an important economic, trade, finance, IT and education centre.

the complex web of existing local interests and relationships.

'It is said in the US that all politics is local – well, in China, all business is local and much of business is political,' says Kedl.

Finding good local legal expertise may be easier said than done, however. The quality of advice and the depth of understanding of a foreign investor's perspective can be variable in the provinces, to say the least. (Even the label 'law firm' can sometimes be misleading. A former journalist who spent time travelling around several smaller Chinese cities while carrying out research for a legal directory tells of her surprise when visiting some law firms. Although describing themselves as firms offering a range of services, at least one turned out to be nothing more than a one-man shop operating from a smoky room above a supermarket.)

The difficult question of *guanxi* appears again here. Some investors may be tempted to rely on a local Chinese lawyer who claims he or she has important connections. This may yield results in the short term but will not provide a stable, long-term base on which to build a business. Harris cites the example of a company that took advice from a local lawyer and rented a property in a small city from a landlord who was not legal. Things went well until the Beijing tax authorities said the company would not be able to claim its rent as a tax deduction because of its illegal landlord.

'I said if you want to feel really bad, the tax authorities might tell Mofcom [the Ministry of Commerce, which regulates foreign companies' operations in China] that you're not operating legally there and you may be shut down.'

Most specialists recommend using a large, national Chinese law firm, preferably one with an office in the same country as the foreign investor, paired with local counsel for certain areas in which local knowledge and connections would really come in useful: filing important paperwork, meeting with local officials, or fighting a case in a local court.

Be open but wary

In conclusion, specialists warn foreign investors against automatically assuming they must invest in Beijing or Shanghai, and say it is wise to be open to other options. But those options should be weighed carefully. Consider your business needs, and the risks involved, and carry out good, thorough due diligence to reduce the chance of creating your own risk.

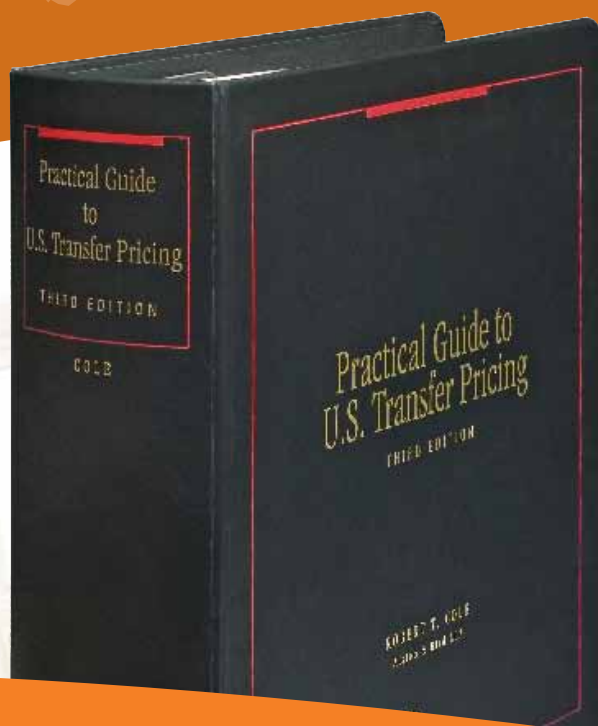
'Don't be scared off – you just need to pay more attention and do more in-depth work to find out who you're dealing with,' says Ho.

'The foreign investor will have to move cautiously since the contemplated investment will be taken in a web of existing local interests and relationships'.

'First off, think. That's right, think,' writes Harris in one of his blog entries. 'Secondly, do not do anything you would not do in any other country. Just because your Chinese partner and/or your Chinese partner's lawyer tell you this is how things are in China does not mean you have to believe them and it certainly does not mean you have to abandon your common sense.' ☒

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A discreet silence

In America, firms compete for controversial and high-profile pro bono matters. In Asia, the same firms have been more pragmatic, tending to keep a low profile. But international law firms may have to strike a balance between commercial interests and the political passions of their Asian employees.

ANTHONY LIN

Last spring's tumult over King & Spalding's withdrawal from representing the US House of Representatives in defence of an anti-gay marriage law served as a reminder of the difficulties American law firms can face when taking on politically controversial matters. In Asia, it also served as a reminder that law firms can take on politically controversial matters in the first place.

Some lawyers in Asia are deeply involved in political controversies, but they are typically not employed by major firms. In China, several human rights lawyers were arrested in a crackdown this spring. Others face ongoing official harassment. The International Bar Association's Human Rights Institute has called for the Chinese Government's persecution of human rights lawyers to end. But the legal profession in Asia itself has been silent on that and other hot topics.

In the United States, firms often compete for controversial but high-profile pro bono matters, like appeals on behalf of death row inmates or Guantánamo Bay detainees. Ask partners from the same firms about their lack of engagement with big issues in Asia and you get different responses. 'Our Asia practices are

mostly transactional, whereas most crusading lawyers are litigators.' 'We are guests here and it would be inappropriate to get involved in our host nation's affairs.' 'We can't do anything that would compromise our ability to service our clients.' 'Are you serious?'

This all makes perfect sense for the firms. But, as with Paul Clement at King & Spalding in the gay marriage law flap, it's usually individual lawyers who drive their firm's involvement in controversial matters. The legal profession has traditionally attracted its share of bright and passionate people. While expatriate lawyers rotating through Asia are unlikely to become activists about anything beyond their tax treatment, top international firms now focus more on building practices in the region with locally recruited lawyers. Can firms operating in Asia really expect these lawyers to remain strictly focused on the work before them and not the world around them?

Perhaps for now. The risk factors are pretty stark, after all. Leaving aside the threats of jail and harassment facing human rights lawyers in China, attorneys at firms would more likely fear the loss of business. Could criticising, say, the Chinese Government lead to less work

from Chinese State-owned companies, or even private companies, foreign and domestic, eager to avoid controversy themselves? Why even chance it?

Still, the imperative to keep one's head down may not always carry the day. The move into Singapore politics by Davis Polk & Wardwell partner Show-Mao Chen offers a hint of the future. A top capital markets partner in Davis Polk's Beijing office, Chen led his firm's work on deals like last year's US\$22bn initial public offering of the Agricultural Bank of China. But earlier this year, he threw his hat in the ring for a parliamentary seat in his adopted homeland of Singapore. And he did it as a member of the opposition Workers' Party (WP).

Singapore is not China, but opposition politicians have faced harassment there, most commonly in the form of libel suits. Politics have long been dominated by Lee Kuan Yew, prime minister from 1959 to 1990 and the 'minister mentor.' The current Prime Minister, Lee Hsien Loong, is Lee Kuan Yew's son; his People's Action Party held 82 out of 84 seats in Singapore's Parliament until May's election. Chen argued that Singapore needed a stronger opposition to increase the ruling party's transparency and

responsiveness, and his presence electrified the campaign. Six WP candidates, including Chen, won seats, the best showing for an opposition party in Singaporean history.

Chen has retired from Davis Polk, which has no Singapore office. If the firm did, it might not be thrilled to have a leading opposition politician as its top partner there, when the Government controls a good chunk of the potential client base through its Temasek Holdings Pte Ltd and Government of Singapore Investment Corporation Pte Ltd (GIC) funds. But the time will come when more international firms may have to strike a balance between their commercial interests and the political passions of their Asian employees.

The outcome of such calculations may seem foregone at the moment. Sometimes, though, it doesn't take

too many politically engaged lawyers to bring change to the status quo. Just ask the voters of Singapore. ☒

Anthony Lin is chief Asia correspondent for The American Lawyer and editor of The Asian Lawyer (www.theasianlawyer.com), where a version of this article first appeared. He can be reached at alin@alm.com.

'Top international firms now focus more on building practices in the region with locally recruited lawyers. Can firms operating in Asia really expect these lawyers to remain strictly focused on the work before them and not the world around them?'





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